

FUNDAMENTALS OF SERVICE TAX

MADE EASY

By

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PREFACE

Service Tax is one area which has seen tremendous changes in the last decade or so since its introduction in the year 1994. One reason for this area to see so many changes has been the contribution of the service sector to our economy. The Government therefore has seen this area as one which can be used to boost revenues in order to meet its expenditure targets. One aspect which merits attention is that despite the contribution of the service sector to our economy in terms of exports, this is one area which has also seen substantial litigation and the service providers not getting their dues mainly because of opposition from the department.

The assesses problems are compounded because they have very few people to turn to in case of need as most of the professionals in the finance field have little knowledge of service tax. This would often result in the assesses either facing an exposure at some point of time or the other or losing out on certain legitimate benefits that they entitled to in complying with the law. Considering the issues being faced by the assesses as well as their counselors, we have thought it worth while to come out with a material which would explain the basic concepts of service tax emphasizing on aspects like levy, classification, valuation, exemptions, export and import of service plus adjudication and appeals. This material does not include a discussion on various individual taxable services considering the fact that there are 107 categories as well as the fact that this is a material aimed at professionals who are unfamiliar with service tax as well as the fact that this is absolutely free!!! The authors are grateful to CA Vinay K.V. for his contribution to editing some chapters of this online book.

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CHAPTER 1. SERVICE TAX - AN OVERVIEW

Tax on services has been in vogue in India since 1994 when it was introduced for the first time. When it was introduced initially there were three services which were liable but over the years various other services have been added and today more than a hundred services are liable under service tax. The basket of services liable to service tax is only expected to grow in the near future as the service sector's contribution to the country's GDP is expected to increase even further though possibly most of the services which can be comprehended are already being taxed. Here, a negative list would make more sense to avoid uncertainty caused by frequent changes.

One of the main reasons for the services to be taxed is the fact that the manufacturing sector can be taxed only to a certain extent if we are to ensure the competitiveness of our industry, since ours is no longer a closed economy, all activities are to bear the burden. Services presently forming more than 55 % of the GDP are expected to reach 70% in the next decade, which should also bear the burden of tax. This tax would be subsumed into the Goods and Service Tax which maybe in place in the next few years.

Levy whether constitutionally valid?

The levy of service tax was initially under the residuary powers conferred to the Union by entry 94 of List I to the Seventh Schedule to the Constitution of India. Later entry 92C was introduced specifically to cover 'Taxes on Services'. In a number of cases the constitutional validity of service tax has been questioned and the decisions of the High Courts/ Supreme Court have been in favour of revenue.

A) In *Tamil Nadu Kalyana Mandapam Assn Vs UOI* ((2004) (167) ELT 3) S C., the levy of service tax on mandap keepers and outdoor caterers was upheld by the Supreme Court as a tax on services and not a tax on sale of goods or hire purchase activities.

B) The levy of service tax on professional services of Chartered Accountant, Cost Accountant and Architect was also upheld by the Supreme Court in *All India Federation of Tax Practitioners Vs UOI* (2007 (07) STR 625-SC).

One thing which is yet to be resolved is the validity of service tax levy on rental of immovable property though the Delhi High Court has admitted a writ petition in *Home Solution Retail India Ltd Vs UOI* (2009-TIOL-196-DEL-HC-ST) challenging the levy of

service tax on pure renting of immovable property without there being a service associated with the renting of immovable property.

What is the concept of “service”?

Assessee should note that in order to attract service tax, there should first of all be a service. The concept of “service” though has not been defined for this purpose under law and one would have to refer the meanings given by dictionary to understand the same.

Composite contracts – Liability.

Service tax is a tax on service and not a tax on sale of goods. The various decisions given by the Courts on the constitutional validity of service tax have also clarified this aspect. At the same time, both sales tax and service tax are mutually exclusive of each other as laid down by the Supreme Court in *Imagic Creative (P) Ltd Vs Commissioner Commercial Taxes* (2008 (9) STR 337 (SC)). There are notifications issued under service tax which provide for deduction / abatement in respect of the transfer of property in goods made during the provision of services and this deduction/abatement would be from the gross value charged for the service. The applicability of these notifications would depend on the nature of the services involved and the activities performed. Before opting for the benefit of these notifications, the assessee should ideally perform a cost-benefit analysis as there are associated conditions to be met to claim such deduction.

Governing provisions

The provisions pertaining to service tax are given in Chapter V and VA of Finance Act 1994 as amended from time to time. The Central Government has also been empowered to make rules to carry out the provisions of this Chapter, through section 94 of this chapter. This comes along with the power to grant exemptions from Service Tax u/s 93. The Government has consequently notified various sets of rules, the provisions of which have been explained as we proceed with this book. The rules which may be noted are as follows –

- Service Tax Rules 1994
- 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

- Taxation of Services (Provided from outside India and received in India) Rules 2006
- Works Contract (Composition Scheme for Payment of Service Tax) Rules 2007

Levy and collection

The levy of service tax extends to whole of India except that it does not extend to a service provider providing taxable services from the state of Jammu and Kashmir by virtue of section 64 of Chapter V of Finance Act.

The question of taxing a service would arise where the service that is provided by the service provider happens to be covered under the various sub-clauses of section 65(105) as a taxable service. Once the relevant clause is identified, the concept of “service provider” and “service receiver” would also have to be satisfied in order to tax the concerned service. In most of the categories though, the “service provider” and the “service receiver” can be any person. In other words, the concept is not restricted to individuals or to firms or to corporate and any one providing the designated services to any person, would be held liable.

Members may note here that the departmental officers have been trying to go one step further and tax agreements for mere sharing of expenses even though there may not be any underlying service involved. Today, taxation of reimbursement of expenses is a major issue which is faced by many multinationals even though the underlying agreement/contract does not bring about a service provider-service receiver relationship between the parties concerned.

Where the criteria set out are satisfied, the tax would be levied on the service provider who would be liable to collect the service tax amount from the service receiver and remit it to the government. However in certain cases the statute requires the service receiver to pay the service tax to the government. The charge of service tax would be at the rates set out in section 66 which is presently 10%. The education and secondary higher education cess would be payable on this amount at 3% and the total service tax including cess is 10.30% as on date though this rate is very likely to go up in future

Since the levy of service tax is on the provision of service, the services provided before the date on which such services were brought under the tax net, would not be subjected to service tax. Readers here may note that even if the bills for the services provided are raised by the service provider after the date on which the service became taxable, there would be no liability as the services had been provided during the period when the

service was not taxable at all. This has been confirmed by the Ahmedabad High Court in *Schott Glass India (P) Ltd Vs Commissioner Central Excise and Customs Vadodara II* (2009-TIOL-82-HC-AHM-ST)

Concept of Classification

The service provider should ensure that he classifies the concerned service properly as this would enable him to ascertain his liability correctly. Correct classification is critical as the exemptions under service tax barring the general exemptions are based on specified categories and if the classification is wrong, the service provider may either end up paying more than required or even face a liability. For the purposes of classification, the category which gives the most specific description of the service should be adopted. Where composite services (involving combination of different services and to be distinguished from composite contracts involving both transfer of property in goods as well as provision of taxable services) are provided, the classification should be on the basis of the service which gives them their essential character. Where the aforesaid two principles cannot be followed for classification, the classification shall be under the sub-clause which occurs first among the sub-clauses which equally merit consideration as per section 65A. In addition to this, the non statutory principles as to consideration of trade parlance especially where certain “terms” are not defined under law would also assume significance as indicated in *CC General (New Delhi) Vs Gujarat Perstorp Electronics Ltd* 2005 (186) ELT532

Registration

Every person liable to pay service tax is required to register himself by making an application to SCE as per section 69. The service provider before registering himself shall ensure that he has crossed the exemption limit of registration for the small service provider which is Rs. 10 lakhs, specified by notification 6/2005 ST dated 01.03.05 as amended from time to time. Branded service providers i.e providing services under brand name or trade name of others, would not be admissible for the exemption. An illustration could be the commercial coaching franchisees. The exemption from registration would not be available for a person who is liable to pay service tax as receiver of services. Moreover, the aggregate value of taxable services provided in the preceding financial year should not exceed Rs. 10 lakhs in order to avail the benefit of this exemption.

As per Rule 4 of Service Tax Rules 1994, an application in Form ST 1 would have to be filed within thirty days from the date on which the taxable service is provided/tax is levied on such service. The assessee would also have the option of going in for centralised registration where the accounting and billing activities are centralised. A change in the information or any additional information sought to be given shall be intimated in writing to the jurisdictional Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise. There is a penalty of Rs. 200 per day or 5000/- whichever is higher for delay in registration.

Concept of consideration and valuation

The service provided should be for a consideration. As per section 67, where the consideration is wholly in money, the gross amount charged for the service would be liable. Even reimbursements of expenses shall be liable as per Service Tax (Determination of Value) Rules 2006 unless the same is incurred by the service provider as a pure agent of the service receiver. The conditions to be satisfied for this are explained in the chapter on valuation. The gross amount charged shall include payment by cheque, credit card, deduction from account and any form of payment by issue of credit notes or debit notes and book adjustment. One would have to refer the Rules on valuation to ascertain the value where the consideration is not wholly or partly in monetary terms or where the same is not ascertainable.

Payment of service tax

The service provider providing taxable services shall be required to pay service tax under section 68(1). However, the service provider does not have to pay service tax until he collects the value of service, from the service receiver towards the taxable services provided by virtue of Rule 6 of Service Tax Rules 1994. Once the payments are received, the service tax shall be paid by the 5th of the month following the month in which the sums are received towards such taxable service. However, in respect of the amounts received in the month of March, the payment would have to be made by the 31st of March and not by 5th of April. Where the payment is made electronically, the due date is 6th of the following month instead of 5th. Receipt of amount towards taxable service though is not a pre-requisite for taxing when the service provider and the service receiver happen to be associated enterprises as defined under Section 92A of the

Income Tax Act 1961. In this case, even debit/credit in the books towards value of service provided would require payment of service tax.

The liability to pay would even arise where the service provider receives amounts in advance towards taxable services to be provided by virtue of definition of Taxable services read with section 67. Where the assessee pays excess service tax as result of collecting amounts in advance from the customer and then not providing the service, the excess amount paid can be set off against the service tax liability for the subsequent period provided the excess service tax collected from the customer has been refunded to him. Where this is not possible, the refund option may be selected and if so, the claim is to be made as per the procedure explained in a later chapter dealing with refund procedure.

Payment of Service Tax by the receiver of service

Generally it is the service provider who provides the taxable services who is called upon to collect service tax from his customer/client and pay the same to the government. But section 68(2) empowers the government to notify the services with regard to which the service receiver would be held liable to pay service tax to the government. The government has consequently notified the following services in this regard through notification 36/2004 ST dated 31.12.2004 as amended from time to time –

- Goods Transport Agency service – specified person paying the freight
- Business auxiliary service of distribution of mutual fund by a mutual fund distributor or agent – mutual fund or asset management company receiving such service
- Sponsorship service provided to any body corporate/firm in which case, the body corporate or firm receiving such sponsorship service would be liable
- Taxable services received by any person in India from abroad – the recipient of such service in India.
- Insurance auxiliary service by an insurance agent – person carrying the general insurance business or life insurance business

Where the service provider pays the service tax to the department and the same is collected by him from the service receiver/customer which may be the case where a GTA service is involved, the service receiver in our view cannot be called upon again by the department to pay service tax as it would amount to double taxation. This view has

recently been followed by the Tribunal in Mandev Tubes Vs CCE Vapi (2009-TIOL-1231-CESTAT-AHM).

Payment of Interest

Section 75 of Chapter V of Finance Act 1994 as amended from time to time provides for payment of interest by the assessee where there is short payment or delay in payment of service tax. The present notified rate is 13% p.a. simple interest as per Notification 26/2004 ST dated 10.09.04 and this should be paid along with the tax. The interest shall be for the period of default.

Cenvat Credit scheme

The service provider providing taxable services is entitled to avail cenvat credit of the service tax paid on input services as well as excise duty charged on inputs and capital goods used for providing such taxable service. This credit can be used by him to pay off his liability on his services. This would reduce his outflow in cash on account of service tax. Eg – If his liability is Rs. 10000/- and he has credits of Rs. 4500/-, he utilizes this and pays only Rs. 5500/- in cash. The credit of service tax on input services (eg. Telephone service, management consultancy, professional services, security service etc) would be available once the payment has been made to the input service provider for the value of services including the service tax amount. Part payment would enable part credit. The service provider would however have to be careful where he provides both taxable as well as exempted services in which case he shall be required to follow Rule 6 of Cenvat Credit Rules 2004 for the purpose of arriving at the correct figure to be claimed as credits.

Export of Services

The service provider who exports his service in accordance with the Export of Service Rules 2005 would not have to pay service tax on such exports. He would also have the option of going in for the rebate of service tax paid on taxable service exported or service tax paid on input services or excise duty paid on inputs used in providing such taxable services exported in accordance with Rule 5 of Export of Service Rules 2005 and the notifications specified thereunder. Another option would be that of refund in accordance with Rule 5 of Cenvat Credit Rules 2004.

Filing of returns

The service provider is required to submit half-yearly returns in Form ST-3 or Form ST-3A (as the case may be) with relevant copies of Form GAR 7, in triplicate by the 25th day of the month following the end of the relevant half-year as per Rule 7 of Service Tax Rules 1994. Form ST-3A is to be used where a deposit is to be made provisionally (i.e. the assessee has opted for provisional assessment). The returns are to be filed for the half year ending 30th September and for the half year ending on 31st March. Where the assessee makes a mistake in the return, the revised return in Form ST 3 should be submitted within ninety days from the date of submission of the return under Rule 7.

Where the filing of the return is delayed, the service provider would have to pay a sum to the credit of the central government as follows under Rule 7C of Service Tax Rules 1994

—

- Rs. 500 for a delay of 15 days from the prescribed date
- Rs. 1000 where the delay is between 15 and 30 days from the prescribed date
- Rs. 1000+ Rs. 100 per day of delay where the delay is beyond 30 days from the prescribed date but not exceeding Rs. 2000 in terms of Section 70.

Rule 7C empowers the Central Excise Officer to reduce or waive the penalty for delayed filing of return, where the gross amount of service tax payable is nil and there was sufficient cause for not filing the return

Service Tax Return Preparer

Section 71 enables the Board to notify a scheme for preparation and filing of service tax returns through a class of persons known as Service Tax Return Preparer authorized for this purpose. The assessee could thus utilize the services of STRP where he has any difficulty in filing the returns. The Government has framed the Service Tax Return Preparer Scheme 2009 notified through Notification 7/2009 ST dated 03.02.09, a copy of which can be obtained on the website www.cbec.gov.in.

Assessment

The assessee is required to assess the tax payable by him and pay the same on monthly or quarterly basis as applicable. In other words, what is envisaged here is self-assessment. Rule 6(4) of Service Tax Rules 1994 enables him to opt for payment on

provisional basis where there is difficulty in ascertaining the amount to be paid. For this, he shall make an application to ACCE/DCCE. The assessment would be finalized at a later date. The departmental authorities can call for further information as they may require from time to time. The provisions of Central Excise Rules would apply here in relation to such provisional assessment with the exception as to requirement of furnishing of bond.

Is best judgement assessment possible under service tax?

Section 72 authorizes the Central Excise Officer to make such assessment after allowing the assessee to represent his case, where the assessee has failed to make service tax returns or assess the tax properly. Thus where the assessee fails to assess tax properly or fail to furnish return itself they could face the risk of the department calling for a best judgment assessment. However these assessments are expected to lead to substantial litigation.

Provisions as to recovery

As per section 73 of Chapter V of Finance Act 1994 as amended, where the service tax has not been levied or paid or has been short-levied or short-paid or erroneously refunded, the Central Excise Officer handling service tax can serve a Show Cause Notice on the person chargeable with service tax as to why he should not pay the amount specified in the notice. The notice shall state the amount involved. This can be done within one year from the relevant date unless such short payment/ non-levy/refund was by reason of fraud or collusion or willful mis-statement or suppression of facts or contravention of the provisions of Chapter V or rules made thereunder with the intent to evade payment of service tax. In such cases, the time limit would be five years.

There is an option of completing the proceedings by payment of the tax amount along with interest u/s 75 before issue of notice in cases pertaining to fraud, collusion etc., by paying the said tax and interest along with penalty of 25% of the service tax specified in the notice within 30 days from the date of communication of notice.

Provisions pertaining to penalty

Section 76 of the Finance Act provides for a penalty in case of failure to pay tax, of an amount equal to the higher of -

1. A sum of not less than rupees two hundred for every day during which the failure to pay tax in accordance with section 68 continues, or
2. Two percent of the tax for every month, starting with the first day after the due date till the date of actual payment of service tax due.

The total amount of penalty cannot exceed the amount of service tax payable.

The penalty in cases of fraud, collusion, willful misstatement, suppression of facts or contravention of any provision with an intention to evade the payment of service tax would be u/s 78. In a case where penalty u/s 78 is imposed, penalty for failure to pay service tax u/s 76 shall not apply. This section even provides for a reduction in amount of penalty to 25% of the service tax determined where payment of tax and interest is made within 30 days from the date of communication of order, along with the penalty so determined.

Provisions pertaining to Appeals

Section 85 of the Finance Act, allows an assessee or revenue aggrieved by any decision or order passed by an adjudicating authority subordinate to the Commissioner of Central Excise, to appeal to the CCE (Appeals) within three months from the date of receipt of the decision of the authority.

Rule 8 of Service Tax Rules 1994 requires the appeal to be made on Form ST-4 in duplicate. A copy of the order sought to be appealed against is also to be filed with the appeal.

Section 86 allows the assessee or revenue to make an appeal to the Appellate Tribunal against the order passed by either the CCE or CCE (Appeals). The appeal is to be filed within three months of the date on which the order sought to be appealed against is received by the assessee and as per Rule 9 of Service Tax Rules 1994, would be filed on Form ST-5 and would be in quadruplicate. Even orders passed either under section 73 dealing with recovery or a revision order of the CCE u/s 84 or order adjudging penalty u/s 83A may be appealed against.

As far as appeals to High Court and Supreme Court are concerned the provisions of sections 35G and 35L of the Central Excise Act 1944 would apply. The appeal to High Court can be made against the order of the Appellate Tribunal once the High Court is satisfied that the case involves a substantial question of law. The appeal shall be within

180 days from the date on which the order appealed against is received by the assessee. The fee shall be rupees two hundred.

The appeal against the order of the High Court shall be with the Supreme Court once the High Court certifies the case to be one that is fit for appeal to Supreme Court. This may be done on its own motion or on an application by the assessee once its judgment is delivered. The decision of the Supreme Court shall be final and binding on the parties concerned. The practice of the revenue department to continue to raise protective demands or litigate a matter much after its judicial confirmation should be discouraged as it amounts to harassment to the tax compliant service providers/ receivers who contribute more than 80% of the total collections of taxes whether in direct or indirect taxes. It would also embrace the global best practice of trusting the tax payer both in word and spirit to reduce the cost of tax administration.

CHAPTER 2. SERVICE TAX - LEVY

The service tax levy is attracted when a taxable service is provided by a defined service provider to a defined service receiver. Unless a service can be regarded as being taxable and being provided by a defined service provider to a defined service receiver, it cannot be taxed. All the three conditions here should be met and even if one of the conditions is not met, the activity in question cannot be taxed. The assessee may however note here that the concept of service receiver now is only of academic interest as the scope of the term is being widened to cover almost all service receivers in the last couple of years (the service receiver can be any person in most of the services). Over the years, the number of services being subject to service tax is also being increased by including all the concerned services in the relevant section discussed above. The service tax levy does not extend to the state of Jammu and Kashmir.

Meaning of the term “service”

The word “service” has not been defined under service tax may be with a purpose. The government can deem any activity or transaction to be a service. One would have to go by the dictionary meaning of the term “service”. Black’s Law Dictionary defines the term “service” to mean an intangible commodity in the form of human effort such as use of labour, skill or knowledge for the benefit of another. One of the meanings given by Webster’s dictionary goes thus – “performance of any duties or work for another; helpful or professional activity”. Where there is no service, there would be no liability and a transaction cannot be deemed to be one involving a service in the absence of service. Moreover, what is not a service is not easy to determine. The revenue seems to be of the opinion that what is not goods is a service as indicated by their efforts to tax supply of goods for use. Even this view was questioned recently by the Delhi High Court which observed that in a pure renting transaction there is no value added service provided at all which in the opinion of the authors appears valid. In any contract, the question as to whether there is any service involved would have to be answered by ascertaining the substance of the contract. If the contract is one where no service is involved, then there cannot be a levy of service tax.

Relevance of the concept of taxable service

The concept of taxable service can be appreciated by going through section 65(105) which consists of various sub-clauses with each sub-clause seeking to define “taxable service” in relation to a particular service category. In order to tax a particular service, the same should be covered by one of the sub-clauses of the above mentioned section. as a taxable service.

Though the service tax levy is attracted at the time of provision of taxable services the payment of the same can be made at the time of receipt of the consideration. But where any amount is received as an advance towards the taxable service to be provided in future, the service provider would be liable to pay service tax on the same. In case the service is not provided at all, the service tax paid in advance would be allowed to be adjusted in the subsequent period or would be refunded.

As per the second proviso to Rule 6(1) of Service Tax Rules 1994, no matter when the payment is received towards the value of services, no service tax shall be payable for the part or whole of the value of services attributable to services provided during the period when such services were not taxable.

The concept of taxable service is also critical as the cenvat credit availment would be on excise duty incurred on inputs and capital goods and service tax paid on input services used for providing such service. Even where the export benefits are to be examined in respect of the services exported, the services exported should be taxable services.

Relevance of the concept of service provider

In addition to the concept of taxable service, one should also be familiar with the concept of service provider. Under service tax there is no uniform definition of the term “service provider” and it varies from one service to another. The concept of service provider has been defined keeping in mind the category of service that is sought to be taxed. For instance, in case of advertising services, the service provider should be an advertising agency. Similarly, in case of services of a technical nature, the service provider would have to be an agency or an engineer depending on the exact nature of the activity that is sought to be taxed.

Normally the service provider who provides taxable services is liable to pay service tax. However, in certain circumstances he could even be liable as a service receiver. These circumstances would be governed by section 68(2) and the categories with regard to

which the service receiver could be liable have already been given in the chapter on overview. Here, the concept of service provider would not be relevant to attract liability.

Therefore in order to tax a particular service, it should find a mention in one of the sub-clauses of section 65(105) as a taxable service plus the person providing the stated service should be covered as a service provider by the relevant definition. Where the service is not covered as a taxable service or where the person providing the service cannot be regarded as a service provider under the relevant definition, the person providing the service would not be liable to service tax.

Very often the confusion regarding the taxability is on account of differences in interpretation of the definitions concerned which can be resolved to a certain extent by strictly going as per the facts and circumstances of each case and by studying proper commercial / business practices.

Relevance of the concept of service receiver

Normally the service receiver is the customer/client who receives the service. Here one should note that a service provider cannot provide service to himself. Thus the existence of the defined service receiver as stipulated by the relevant definitions would also be necessary to attract liability. Now with most of the service receivers being “any person” only the cases where it is different would be relevant.

Where service provider is also a manufacturer – whether service tax levy would apply

It is quite possible for a service provider to also be engaged in manufacturing activities. But the fact that he is a manufacturer would not alter his liability under service tax especially where the manufacturing activity and service related activities are two separate streams of activities having no bearing on each other. Even where the activities are inter-linked, the liability under service tax could be unaffected by the liability under Central Excise if the goods are sold to the customer on being manufactured and service is provided subsequent to such sale.

The situation could be different in case of composite contracts dealing with the supply of manufactured goods and provision of services in relation to the same, where the amounts cannot be bifurcated in terms of material supply and provision of services. In this case the service provider would have to proceed taking into account the exemptions

/ abatements available under service tax, the deduction available under the VAT law of the concerned state, his cost break up in terms of material and labour components apart from his customer's business profile. An example could be the contractors involved in windows, glazing and building facades. They could ideally remove the goods manufactured in their unit on comparable values discharging the CE duty at the applicable rate. The service division would avail the credit of such duty along with other input services and use the same to discharge the ST on the whole value of the contract. This would enable encashing the duty paid on manufacture and should be possible in the opinion of the authors. This option would be useful where the customer is eligible for credits.

Pointers for practice

- The professional here would have to have a fair idea as to the provisions prevailing under the VAT law of the concerned state if he is really to add value to his client's business. This would be so, as the more appropriate course of action is to be selected from a given set of alternatives. This would involve the study of deductions available for labour as per the VAT law, composition benefits, deduction for materials transferred under service tax, conditions to be met in order to claim deductions etc.
- The professional would have to go through the agreements the client has with his customers so that the essence of the same could be understood. This is critical in order to determine the liability or the absence of one under service tax.
- It may also be important to examine the taxation of the incoming services/ goods as well as the customers' liability to central excise duty or service tax.

CHAPTER 3. CLASSIFICATION OF SERVICES

Classification of the service involved under service tax is perhaps the single most important step in ensuring legal compliance. Classification of services poses certain challenges unlike classification of goods as services are intangible. Professionals handling service tax matters often face problems here as the service sector involves specialists who specialise in certain select fields (technocrats, scientists, engineers) and who are not attuned to the requirements under service tax and the possible ramifications of non-compliance. Sometimes, the service provider may even be uneducated (for instance if he is a goods transport agency, sub contractors in the construction industry, pandal or shamiana contractor). Very often when it comes to classifying a service, difficulties are faced in understanding the exact nature of services being provided by the service providers as the explanations given can only be understood by another technically qualified individual rather than a professional who is well versed only in matters pertaining to taxation. The understanding of the trade is critical in this regard.

Relevance of the concept of classification

An assessee under Central Excise would know the importance of classification and the influence it would have on his liability. Similarly the importance of classification under service tax is not to be underestimated. There have been numerous instances of the assessee's differing with the departmental authorities on the issue of classification of services that they provide.

Under service tax, correct classification is the single most critical factor the assessee should take care of if he is to feel secure as far as his compliance is concerned. This is for the reason that the various categories of services have been brought under the tax net over a period of time beginning with the year 1994 rather than in one shot. Thus when the assessee considers the various alternative categories for classifying his services, he may be confronted with a scenario where two or more services are liable from different dates. This would substantially increase the risk factor of non-compliance arising from improper classification of the service.

For the purpose of classification, one would have to follow section 65A of Chapter V of Finance Act. As per this section, the classification of the service has to be determined keeping in mind the sub-clauses of section 65(105). That is, in order to classify the services provided, the assessee is supposed to have a fair knowledge of the categories that are taxed under the aforesaid section and he should be able to identify the possible categories that could apply in his case and select the one that is most appropriate. The view of the revenue is normally available in the Circulars and if within that boundary of law, the service provider would be safe and is advised to follow the same.

The classification is done following the principles laid down below –

- The sub-clause which provides the most specific description shall be preferred to sub-clauses providing a more general description. This has also been upheld by the Punjab and Haryana High Court in Dr Lal Path Lab (P) Ltd vs CCE Ludhiana (2007 (08) STR 337 (HC-P&H)).
- Composite services consisting of a combination of different services, which cannot be classified as per the aforesaid clause, shall be classified as if they consisted of a service which gives them their essential character
- Where a service cannot be classified as per the aforesaid two clauses, it shall be classified under the sub-clause which occurs first among the sub-clauses which equally merit consideration

Possible ramifications where the assessee gets the classification wrong

Where the assessee gets the classification of service wrong, the result could be as follows –

- Losing out on the exemptions which could have been claimed if the classification had been done correctly, as a result of which the assessee pays more than what is required to be paid
- Loss of business due to rivals/competitors being cost-effective
- Wrongly claiming exemption that he was not entitled to in the normal course as a result of which he is saddled with additional liability along with interest and penalties which cannot be collected from clients/customers thereby affecting his cash flows

- Paying service tax when he was not required to pay as a result of wrongly classifying his service under a category which was not appropriate leading to huge debts. He could lose where the refund period of 1 year would also be over.
- Not paying service tax when he was actually liable to pay the same as a result of classifying his service under a category which was not being taxed earlier but is taxed from a later date.
- Getting the liability on Import of Services all wrong or not claiming the benefit of export on service exports due to improper classification could also happen. This could happen when the alternative headings available have different import/export criterion being applicable to them.

Pointers for practice

- The professional handling service tax matters would be required to go through the various records maintained by the assessee before arriving at a final decision regarding classification. This would ensure that the classification is done on the basis of documentary evidence rather than only on the basis of interviews. However in the absence of documents the same maybe made clear in the opinion.
- The professional would have to be careful in case of composite services. Here, the agreement available or the method of invoicing or charging need not in itself determine whether the service is a single service or multiple services. Here, the real nature and the substance of the transaction should be the guiding factor rather than form of the transaction, for the purposes of classification. He/she should therefore try to find out the category of service which gives the essential character and then adopt that category for classification
- Periodical review of the classification may also be undertaken by the professional to ascertain whether the concerned services can be classified under other headings which have been introduced at a later date and which provide a more specific description of the concerned service. This possibility cannot be ruled out though it may be remote. The shelf life of the opinion is to made clear to the client.

- In case of any doubt in the classification, the same is preferable to be intimated to the department and their confirmation sought. This would also allow for amendment in future when the matter becomes clear.

CHAPTER 4. CENVAT CREDITS AND PAYMENTS

Introduction

The concept of VAT provides that the indirect taxes paid in the earlier point of time are allowed to be set off against the tax payable at a later point of time. It may also require that the chain is not broken for maximisation of the gain under this scheme. The credits are available to the service provider and consequently awareness of the provisions as well as the procedures is to be ensured for effective compliance under service tax. Assesseees who are new to both central excise as well as service tax should note that cenvat credit scheme is a scheme which provides for a scheme of set off of the Central Excise duties on inputs and capital goods and service tax paid on input services against the liability arising on taxable services or excisable goods. Thus where a service provider uses certain materials which have suffered duties of Central Excise at the time of procurement, for the purpose of providing a taxable service on which he is liable to pay service tax, the Central excise duties can be set off against the service tax liability. This set off facility would also be available in respect of service tax paid on input services used for providing the taxable service.

The set off scheme talked about above is presently governed by the Cenvat Credit Rules 2004 which is common to both assesseees under Central Excise as well as Service Tax. The Rules provide for cross-sectional credit i.e a service provider not only gets credit for the service tax paid on input services but even for Central Excise duties on raw materials and capital goods used for providing the taxable service. The present sets of Rules are in force from 10th of September 2004 which is also the date from which the cross-sectional credit is admissible. The effect of these Rules would be to reduce the cash outflows for the service provider on account of service tax. An example would clarify this

Example – Ms. Nagabhushan Associates is a service provider whose service tax liability is Rs. 150000 and the service tax paid on input services like consultancy fees, technical testing, professional fees and security services put together is Rs. 65000 and the Central Excise duties on the raw materials and capital goods as shown by the suppliers' invoices are Rs. 35000. If the opening balance of credits from the previous months is Rs. 10,000 the calculation of the service tax amount to be paid by Ms. Mahadev Associates in cash is as follows –

<i>Particulars</i>	<i>Amount Rs</i>	<i>Amount Rs</i>
Service tax liability as stated above		150,000
<i>Less: - Credits available for set off</i>		
Opening balance of Cenvat credits	10,000	
(+) Cenvat Credit on raw materials and capital goods	35,000	
(+) Cenvat credit in respect of input services	65,000	
Total credits available for set off	110,000	
Deducting the credits total from the service tax payable		(-) 110,000
Amount of service tax to be paid in cash		Rs. 40,000

But for the set off available in the above example, the service provider would have had to pay Rs. 150000 in cash which would also have increased the cost of his services to his customer. The Cenvat credit can be utilized only to the extent such credit is available on the last day of the month, for payment of duty or tax relating to that month.

The Cenvat Credit Rules 2004 specify the duties and the taxes which can be used for set off as well as the conditions to be followed by the service provider in order to claim these credits set offs. The credits would not be available in respect of the Central Excise duties on raw materials and service tax on input services used for providing an exempted service. *In respect of capital goods, the credit of CE duties on such capital goods can be denied where they are used exclusively for providing exempted services.* Moreover, in respect of the service tax on input services, the credits would be admissible only on payment of service tax and the value of service to the input service provider and not before that. This restriction applies only to input services and not to inputs and capital goods.

Before we proceed with the discussion on Cenvat Credits, it is important to consider some of the critical definitions as relevant to a service provider. In this regard, the definitions of “input”, “input service” and “capital goods” assume significance. The reader

is advised to refer the Cenvat Credit Rules 2004 for the exact text though the definitions have been discussed below with reference to a service provider.

Concepts

Concept of input

“Inputs” generally mean all goods used for providing any output service. “Inputs” would not include light diesel oil, high speed diesel oil and motor spirit and motor vehicles.

Concept of output service

“Output service” as per Rule 2(p) of Cenvat Credit Rules 2004, means any taxable service provided by the provider of taxable service, to a customer, client, subscriber, policy holder or any other person as the case may be. Taxable service shall not include service where the receiver pays the tax like GTA, sponsorship or import of services. Therefore where the receiver is required to pay the service tax, the same has to be paid fully in cash. The logic is that an input service credit cannot be used to pay the service tax on another input service.

Concept of capital goods

“Capital goods” as per Rule 2(a) of Cenvat Credit Rules 2004, means the following goods –

1. All goods falling under chapters 82, 84, 85, 90, heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804 of the First Schedule to Central Excise Tariff Act
2. Pollution control equipment
3. Components, spares and accessories of the goods specified at clauses (1) and (2) above
4. Moulds and dies, jigs and fixtures
5. Refractories and refractory materials
6. Tubes and pipes and fittings thereof; and
7. Storage tank

The aforesaid items should be used for providing output service.

Motor vehicles would also be regarded as capital goods where they are registered in the name of the service provider who provides output services falling under the categories stated below –

1. To a customer by a courier agency in relation to door-to-door transportation of time sensitive documents, goods or articles
2. To any person by a tour operator in relation to a tour
3. To any person by a rent-a-cab scheme operator in relation to the renting of a cab
4. To any person by a cargo handling agency in relation to cargo handling services
5. To a customer by a goods transport agency in relation to transport of goods by road in a goods carriage
6. To a client by an outdoor caterer
7. To a client by a pandal or shamiana contractor in relation to a pandal or shamiana in any manner

The definition of capital goods under Companies Act 1956 or under Income Tax Act 1961 would not be valid here.

“Input service” means any service used by a provider of taxable service for providing an output service;

It includes services used in relation to –

- Setting up, modernization or renovation or repairs of the 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
- Activities relating to business (such as accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry and security)
- Inward transportation of inputs or capital goods
- Outward transportation up to the place of removal

Readers may note that the concept of “input service” is usually subject matter of maximum litigation under Service Tax. This is mainly on account of a narrow interpretation of the definition from the departmental officials with the intention to deny credits to the assessee. This has resulted in unnecessary litigation in many cases which are usually resolved by the Tribunal with most of the verdicts being in favour of the assessee. The input services which are usually questioned are – telephone services,

canteen services, rent a cab services, repairs and maintenance of assets, services of outward transportation, etc. We therefore provide you with certain important case laws at the Tribunal level which can be relied upon by the assessee when the need arises.

Case Laws on Input service Credits -

Case Law	Issue decided
GTC Industries Ltd Vs CCE Mumbai V (2008 (12) STR 468 (Tri-LB))	Every clause of the statute should be construed with reference to context in which it is issued - Bare mechanical interpretation of words and application of legislative intent, devoid of concept and purpose reduces most of the remedial and beneficial legislations to futility. Catering service provided by an outdoor caterer was held to be input service relating to business and the expenses thereto forming part of the cost of production.
Sanghi Industries Ltd Vs CCE Rajkot (2009 (236) ELT 617 (Tri-Ahmd))	Input service credit for overhauling of DG set installed in plant was held to be admissible
Millipore India Ltd Vs CCE Bangalore (2009 (236) ELT 145 (Tri-Bang))	Input service - Medical and personal accident policy, group personal accident policy, insurance, personal accident policy, personal vehicle services, landscaping of factory garden and catering bills - Impugned items considered for costing final product in terms of CAS-4, therefore, contention that these services received in relation to manufacture of final product - Credit admissible. Even landscaping the surroundings of factory to be considered as 'input service'
Aditya Birla Nuvo Ltd Vs CCE Bhavnagar (2009 (14) STR 304 (Tri-Ahmd))	Input service – Credit of tax paid on merger charges, charges for issuance of NOC by bank, annual custody fees and maintenance of fax machine at house of company's executive – Plea that mergers come in category of financing, NOC of bank when company wants to borrow also a financing activity, custody fees connected with share registry, being one of the activities of registrar and that maintenance of fax chargers admissible because credit of tax paid on telephone

	admissible – Services covered by categories of services enumerated in the definition of input service under Rule 2(l) of Cenvat Credit Rules, 2004 which may not be considered as directly or indirectly relatable to manufacture but yet intention was to provide benefit of credit – Credit available
M/s ABB Ltd Vs CCE & ST Bangalore (2009-TIOL-830-CESTAT-Bang-LB)	Expression “activities relating to business” has a wide import and includes both essential and auxiliary activities of business including outward transportation. Definition of “input service” has to be interpreted in the light of requirement of business and it cannot be read restrictively so as to confine only up to the factory or up to the depot of manufacturers. Services received for outward transportation of goods from the place of removal is input service.

Duties/taxes which can be considered for set off or availing credits

The duties and taxes which can be considered as per Rule 3(1) of Cenvat Credit Rules 2004 for set off or availment are as follows –

- Basic Excise Duty (First Schedule to CETA)
- Special Excise Duty (Second Schedule to CETA)
- Education cess on excisable goods and on taxable services
- Secondary Higher Education Cess of excisable goods and on taxable services
- Service tax u/s 66 of Chapter V of Finance Act
- Counter Veiling Duty u/s 3 (3) of Customs Tariff Act on imported goods

The aforesaid duties should have been incurred on input or capital goods received in the premises of the provider of output service on or after 10.09.2004 and the taxes should have been paid on any input service received by the provider of output services on or after 10.09.2004.

The service provider cannot claim credit of additional duty (SAD 4%) leviable under section 3(5) of the Customs Tariff Act, by virtue of proviso to Rule 3(1) of Cenvat Credit Rules 2004.

Utilisation of the credits

The service provider who avails Cenvat Credit on inputs, capital goods or on input services can utilize the credits as per Rule 3(4) of CCR 2004, either for –

Payment of excise duty on any final product or

Reversal of Cenvat credit availed on inputs when the inputs are removed as such or after partial processing (other than for providing taxable services) or

Reversal of Cenvat credits or

Payment of service tax on output service or

Reversal of Cenvat credit on capital goods where the capital goods have been removed as such other than for providing taxable services

Education cess and secondary higher education cess credit can be utilized for payment of the Cess on service tax or cess on excisable goods. But the credits of education cess and SHE cess cannot be used for payment of any other tax or duty. Education cess credit is to be used for payment of education cess and SHE cess credit is to be used for payment of SHE cess.

When inputs/capital goods are removed outside the premises

As per Rule 3(5), when inputs or capital goods on which cenvat credit has been taken, are removed as such from the premises of the service provider, the cenvat credit availed would have to be reversed unless the removal was for providing taxable service. Where the removal of capital goods or inputs is for providing an output service, there would be no time limit for receipt of the same back into the premises of the service provider. However, the service provider is advised to track the movement of inputs and capital goods using challans and registers to avoid flouting of Rules and end up with disputes/demands. In case of capital goods removed after use, where the credits are to be reversed, the reversal would be reduced to the extent of 2.5% per quarter of use of the capital goods.

As per Rule 3(5B), where the value of any input or capital goods (before being put to use) is written off fully or provision for writing off fully is made in the books of accounts, the Cenvat credit taken (if any) on such inputs or capital goods would have to be reversed. The credit can be claimed again where such inputs or capital goods are used in providing taxable service.

Restriction in case of capital goods

As per Rule 4(2)(a) of CCR 2004, the cenvat credit in respect of capital goods received in the premises of the service provider who provides taxable services, shall be taken for an amount not exceeding 50% of the duty paid on such capital goods in the same financial year and the balance in the subsequent financial year if the capital goods are in possession of such service provider. The criterion as to possession would not apply to components, spares, accessories, refractories and refractory materials, moulds, dies and goods falling under heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804 of First Schedule of Central Excise Tariff Act. Moreover, in case the capital goods are cleared as such in the same financial year (initial year), the balance can be claimed in that year itself.

Where cenvat credit is claimed on capital goods, the duty amount cannot form part of the cost of the capital goods for the purpose of claiming depreciation u/s 32 of Income Tax Act 1961 by virtue of Rule 4(4) of CCR 2004. If depreciation is claimed on the duty amount on which cenvat credit had been claimed earlier, the credit would have to be reversed.

Capital goods may even be acquired on lease, hire purchase or loan agreement from a financing company u/r 4(3) and credits would still be available as long as documentation is in order.

Can the inputs or capital goods on which cenvat credit is claimed, be sent out to a sub contractor for processing?

The input or capital goods on which credit has been claimed, can be sent out under Rule 4(5)(a) of Cenvat Credit Rules 2004 to a job worker for processing, testing, re-conditioning etc. The goods after processing, testing etc are to be received back within the premises of the service provider within 180 days from the date of sending the same. Where it is not so received, the cenvat credits availed earlier in respect of the inputs so sent would have to be reversed which can again be claimed back once the goods are received any time after the expiry of the said period of 180 days. There is no restriction as to receipt within 180 days in case of capital goods as the same has been amended with regard to a service provider, as long as the removal is for providing output service.

The goods are normally sent under a pre-numbered challan which would consist of details like, name and address of the job worker, the description of the goods, value with duty amount, nature of processing required and the date on which the items are expected. The challan can have a provision for authenticating the receipt and despatch details at his end along with details of dispatch like, goods sent back, scrap generated if any, processing undertaken, date of sending and details of invoices raised if any. The service provider can also maintain a register to keep track of material movements showing the issue and receipt details.

Cenvat Credits – Refund for exporter of service

As per Rule 5 of CCR 2004, where any input or input service is used in providing an output service which is exported (in accordance with the Export of Service Rules 2005), the Cenvat credit in respect of that input or input service can be utilized by the provider of output service towards payment of service tax on taxable services provided within India. Where such utilization is not possible, the provider of output service can opt for a refund of such amount subject to conditions notified by the Central Government.

This refund shall not be allowed where the provider of output service avails of either –

- Drawback under the Customs and Central Excise Duties drawback rules 1995 or
- Claims rebate of duty under Central Excise Rules 2002 or
- Claims rebate of service tax under Export of Services Rules 2005 in respect of such duty/tax.

Where the service provider has both taxable as well as exempted services

The provisions are governed by Rule 6 of Cenvat Credit Rules 2004. Where a service provider exclusively provides exempted services, he cannot avail and utilize the cenvat credits. The same philosophy would also apply to a manufacturer manufacturing exempted final products exclusively.

In a scenario where the service provider provides both taxable as well as exempted services and avails Cenvat credits on inputs and input services used in providing services, he would in the normal course be required to maintain separate accounts for receipt, consumption and inventory of inputs and input services meant for use in

providing output service and those inputs and input services meant for use in providing exempted services. This would be to ensure that he does not claim credits on inputs and input services used for providing the exempted services. Even where they are availed, the same can be reversed in the books.

But where the service provider is not in a position to maintain separate accounts or has not maintained separate accounts, he cannot utilize the full amount of cenvat credits at his disposal. In such a scenario, the position would be as explained below -

For the period prior to 1st April 2008,

The utilization shall be only to the extent of an amount not exceeding twenty per cent of the *amount of service tax payable on taxable output service*. This utilization is subject to having sufficient balance of cenvat credits on hand on the basis of the invoices given by the input service provider/suppliers. The balance credit left out after such utilization can be carried forward to the subsequent period.

On or after 1st April 2008,

The rule now gives the service provider two options –

- Pay an amount equal to 6% (prior to 07.07.09, the rate was 8%) of the value of the exempted services or
- Pay an amount equivalent to the Cenvat credit attributable to inputs and input services used for providing exempted services as per the formula/method indicated

As per this formula/method, the cenvat would be determined in two steps. First of all, during each month, the cenvat credits attributable to exempted activity would have to be ascertained provisionally by taking the value of exempted services, goods manufactured and taxable services *provided during the preceding financial year as the basis*. Secondly, the actual credits that the service provider is entitled to, would be calculated at the end of the year on the basis of actual figures for the relevant financial year with regard to the value of exempted services and taxable services provided or goods manufactured (if any).

Where the credits ascertained finally in relation to exempted activity are less than the credits ascertained provisionally, the service provider can take credit for the differential amount.

Where the credits ascertained finally in relation to exempted activity are more than the credits ascertained provisionally, the service provider would have to pay the differential amount on or before the 30th June of succeeding financial year. Where the payment is made after 30th of June, interest at 24% p.a. would be payable for the period of delay.

The calculations / steps to be taken every month for ascertaining provisional credits in relation to exempted activity would be as follows -

1. Ascertain the cenvat credit attributable to inputs used for manufacturing exempted goods if any and let the credits be A. (This point would apply where a service provider also engages in manufacturing)
2. Ascertain the cenvat credits provisionally in respect of inputs used for providing exempted services as follows – $(B/C) \times \text{Total credits taken during the relevant month}$ not including amount A indicated above.

For this purpose, B = total value of exempted services provided during the preceding financial year

C = total value of dutiable goods manufactured and removed during preceding financial year + total value of exempted services and taxable services provided during preceding financial year.

3. Ascertain the cenvat credits attributable to input services used for providing exempted services or for manufacturing exempted goods as follows – $(E/F) \times \text{Total credits taken during the relevant month}$

For this purpose, E = total value of exempted goods manufactured and removed during the preceding financial year + total value of exempted services provided during the preceding financial year.

F = total value of dutiable goods and exempted goods manufactured and removed during preceding financial year + total value of exempted services and taxable services provided during preceding financial year.

At the end of the relevant financial year, the following calculations would have to be made –

- 1 Ascertain the cenvat credit attributable to inputs used for manufacturing exempted goods if any and let the credits be H. (This point would apply where a service provider also engages in manufacturing)

2. Ascertain the cenvat credits in respect of inputs used for providing exempted services during the financial year as follows – $(J/K) \times \text{Total credits taken during the relevant financial year not including amount H indicated above.}$

For this purpose, J = total value of exempted services provided during the relevant financial year

K = total value of dutiable goods manufactured and removed during relevant financial year + total value of exempted services and taxable services provided during relevant financial year.

3. Ascertain the cenvat credits attributable to input services used for providing exempted services or for manufacturing exempted goods as follows – $(E/F) \times \text{Total credits taken during the relevant financial year}$

For this purpose, E = total value of exempted goods manufactured and removed during the relevant financial year + total value of exempted services provided during the relevant financial year.

F = total value of dutiable goods and exempted goods manufactured and removed during relevant financial year + total value of exempted services and taxable services provided during relevant financial year.

Value for this purpose shall have the meaning assigned in section 67 of Chapter V of Finance Act for service tax and section 4 or 4A of Central Excise Act 1944 with regard to goods.

Example –

If the sale of exempted goods during 2007-08 had been Rs. 150 Lakhs and clearance of dutiable goods had been Rs. 187 lakhs during the said year and the exempted services had been Rs. 45 Lakhs and taxable services had been Rs. 25 lakhs for 2007-08, and the input credit total for the month of April 2008 is Rs. 22 Lakhs out of which the credits on inputs used for exempted goods is Rs. 2.5 Lakhs, the determination for April 2008 would be as follows –

Step 1: - Credits on inputs used for exempted goods = Rs. 2.5 L

Step 2: - Credits on inputs used for exempted services = Rs. 3.41440.

Credits for April 2008 (excluding step 1 credits) $\times$ Exempted services for last year / (Dutiable goods value + Taxable service value + Exempted service values for last year) = $(22 - 2.5) \times (45) / (187 + 45 + 25)$

Step 3: - Input service credits is nil here.

Therefore, the total credits which can be claimed in April 2008 = Rs. 22-2.5-3.41440 = Rs.16.08560 L

If we assume that input service credit of Rs. 4 L is also available, then

Step 3: - Credits on input services used for exempted goods and exempted services = Rs. 1.91646

$$\frac{(\text{Credits for April 2008}) \times (\text{Exempted services value} + \text{Exempted goods values for last year})}{(\text{Dutiable goods value} + \text{Exempted goods value} + \text{Exempted service value} + \text{Taxable service value for last year})} =$$
$$4 \times (45 + 150) / (187 + 150 + 45 + 25)$$

Therefore the credits admissible on input services would be Rs. 4-1.91646 = Rs.2.08354 L.

Note: - The method can also be used by manufacturers under Excise and they would be required to pay 5% (10% before 07.07.09) of the value of the value of exempted goods instead of 6% (of value of exempted services) for service providers. The other option would be the same as discussed above i.e ascertaining the credits as per the method prescribed. If one analyses the method, it would cover even a case where a service provider also happens to engage in manufacturing while the old rule was silent regarding the treatment to be adopted in such cases. Moreover, the segregation is only in respect of inputs and input services and not capital goods. The question of denial of credits on capital goods would arise only where they are used exclusively for exempted goods or exempted services. The option to either go in for the method discussed above or not should be exercised by the assessee once and cannot be changed for the remainder of the financial year.

Another aspect which merits attention here is the treatment to be given to trading activity. Where for instance the service provider apart from providing taxable services also engages in trading activity, whether full cenvat credits can be claimed? Professional opinion is divided in this regard. Authors view is to regard trading activity as being

distinct from exempted activity as what is spoken of in Rule 6 is exempted service or exempted goods and trading cannot fall under either of the two categories. This view has also been followed by Commissioner (Appeals) Central Excise Pune in Faber Heatcraft Industries Ltd case (2008 (12) STR 252 (Commr-Appeals)). The other view would be the conservative view of regarding the same as something not entitling the assessee to credits which would find favour with the department. The authors in their humble opinion though favour the former over the latter as long as the service provider provides taxable services as well.

The third aspect which would require attention is the treatment to be given to opening balances of credits where the service provider switches over from one method to another under Rule 6. The authors are of the view that in the absence of anything specific in Rule 6, the opening balances would be outside the purview of the calculations using the formula given as those balances would be available for utilization.

Treatment under Rule 6 of CCR 2004 where the input services happen to fall under the specified categories

Where the input services obtained by the service provider happen to fall under the categories specified u/r 6 of CCR 2004, full cenvat credit can be utilized in respect of the service tax paid on such services unless such services are used exclusively for providing exempted services or exempted final products by the assessee. In other words neither the restriction as to 20% of the tax payable on output services (for the period prior to 1st April 2008), nor the restriction under the new sub rule 3 and 3A of rule 6 for the period following 1st April 2008, would apply to these services received by the service provider.

The concerned input services are as follows –

1. Consulting engineer's services (Sec. 65(105)(g))
2. Services received from an architect (Sec. 65(105)(p))
3. Interior decorator's services (Sec. 65(105)(q))
4. Management consultant's services (sec. 65(105)(r))
5. Real estate agent's services (Sec. 65(105)(v))
6. Security agency's services (Sec. 65(105)(w))
7. Services provided by a scientist or a technocrat in relation to scientific or technical consultancy (Sec. 65(105)(za))
8. Banking and financial services (Sec. 65(105)(zm))

9. Insurance auxiliary services concerning life insurance business (Sec. 65(105)(zy))
10. Erection, commissioning and installation services (Sec. 65(105)(zzd))
11. Management or maintenance or repair service (Sec. 65(105)(zzg))
12. Technical testing and analysis agency's services (Sec. 65(105)(zzh))
13. Technical inspection and certification services (Sec. 65(105)(zzi))
14. Banking or other financial services by a foreign exchange broker (Sec. 65(105)(zzk))
15. Commercial or industrial construction services (Sec. 65(105)(zzq))
16. Intellectual property services (Sec. 65(105)(zzr))

Service providers may note that the category of works contract service, as well as some of the other construction related services are conspicuous by their absence. This is so while commercial or industrial construction services do find a mention. It is common that as additional services have been included under tax net, their additions in the facilitating segments has been ignored. Whether this is an unintended omission or not is something which would have to be clarified in due course of time but indicates the lack of professional approach to law making in our country.

Where the assessee is both a manufacturer as well as a service provider

Strictly speaking, Rule 6 of CCR 2004 did not specifically cover a scenario for utilization of credits where the assessee engaged in manufacturing as well as providing services and had both dutiable and exempted goods as well as taxable and exempted services prior to 1st April 2008. However, with effect from this date, Rule 6 of the Cenvat Credit Rules 2004 has been amended by indicating the formula to be used for finding out the Cenvat credits attributable to exempted services and exempted goods, which seems to take care of this issue.

Documentation work to be done

The service provider should ensure that he claims the cenvat credits on a valid document satisfying the requirements of Rule 9 of Cenvat Credit Rules 2004. The documents may be -

- An invoice issued by a manufacturer
- An invoice issued by an importer

- An invoice issued by a registered first stage or second stage dealer
- Supplementary invoice issued by a manufacturer/importer
- Bill of entry
- Certificate issued by an Appraiser of Customs in respect of goods imported through a Foreign Post Office
- A challan evidencing payment of service tax where the service receiver is liable to pay u/s 68(2)
- An invoice, bill or challan issued by a provider of input service on or after 10.09.2004
- An invoice, bill or challan issued by an Input Service Distributor

The service provider would also be better off maintaining a cenvat credit register disclosing the details as to the cenvat credits being claimed. The register can disclose details as to the name of the supplier/input service provider, bill number, date, basic value of duty/tax, education cess, SHE cess, assessable value, GRN reference for material receipts, payment reference for input services, column for debits, credits balance. This record would facilitate the task of preparation of returns which would then be easier.

Where the assessee opts for ascertaining the credits as per the method prescribed under Rule 6 of CCR 2004 on a provisional basis

The following particulars would have to be intimated to the Superintendent of Central Excise while exercising this option –

- Name, address and registration number of the provider of output service/manufacturer of goods
- Date from which the option is to be exercised
- Description of dutiable goods or taxable services
- Description of exempted goods or exempted services
- Cenvat credit of inputs and input services lying in balance as on the date of exercising the option under this condition

Once the credits have been determined finally and the excess credits availed paid back or credits short availed have been availed, the following details would have to be sent to the SCE within 15 days from date of payment or adjustment –

- Cenvat credits attributable to exempted goods and exempted services for the whole financial year, determined provisionally on monthly basis
- Credits attributable to exempted goods and exempted services for the whole financial year determined finally
- Amount short paid with the date of payment of the said amount
- Interest payable and paid on the shortfall
- Credits taken on excess payments made earlier

Payment of service tax

The payment of service tax is to be made to the credit of the Central Government by the 5th of the month immediately following the calendar month (6th of the succeeding month instead of 5th if payment is made electronically) in which the payments towards taxable services are received, as per Rule 6 of Service Tax Rules 1994. For the period ending March 31st, the payment would have to be made by the 31st of March and not by 5th of April of the calendar year.

In case the service provider happens to be an individual, proprietary firm or a partnership firm, the payment has to be made by the 5th of the month immediately following the quarter (6th of the month succeeding the quarter if payment is made electronically) in which the payments towards taxable services are received. The cenvat credits position consequently would be determined as at the end of the relevant month/quarter as the case may be depending on the payment period.

Assessees paying service tax of more than rupees fifty lakhs would have to do so through internet banking.

Assessees would also have the option to pay service tax in advance and then adjust the amount paid towards the service tax liability on services provided. Intimation would have to be given to the SCE within 15 days once payment is made. For this, rule 6(1A) has been introduced in Service Tax Rules 1994.

Can Cenvat credits be transferred?

As per Rule 10(2) of Cenvat Credit Rules 2004, where a provider of output service shifts or transfers his business on account of change in ownership or on account of sale, merger, amalgamation, lease or transfer of business to a joint venture, with the specific provision for transfer of liabilities of such business, then such provider of output service

shall be allowed to transfer the Cenvat credit lying unutilized in his accounts, to such transferred, sold, merged, leased or amalgamated business.

The stock of inputs as such or in process or the capital goods are also to be transferred to the new site/owner and the accounting of such inputs/capital goods should be to the satisfaction of the Assistant Commissioner of Central Excise/Deputy Commissioner of Central Excise.

Can the old balance of Cenvat Credit be brought forward?

The service provider can bring forward the unutilized credits lying in his books as on 10.09.04 in respect of the credits availed under Service Tax Credit Rules 2002 and utilize the same in accordance with these rules.

Can credits be taken on inputs and capital goods received under invoice, bill or challan issued by another office of service provider?

Rule 7A of CCR 2004 allows distribution of credits on inputs by the office or another premises of output service provider. Here, the credits can be taken on inputs as well as capital goods received on basis of an invoice or a bill or challan issued by an office or premises of the said provider of output service which receives invoices towards purchase of inputs and capital goods. The assessee would have to note that provisions applicable to first stage and second stage dealers under Central Excise have been made applicable in regard to the office issuing such invoice/bill and distributing credit.

Confiscation and penalty in case of wrong availment of Cenvat Credits

As per Rule 15 of CCR 2004, where cenvat credit in respect of inputs or capital goods is taken wrongly or in contravention of these Rules, then such inputs or capital goods shall be liable to confiscation and the penalty would be Rs.2000/- or duty on such goods whichever is greater.

Where credit on input services has been taken wrongly or sought to be utilized by way of fraud, collusion, willful mis-statement or suppression of facts or through contravention of any of the provisions of the Finance Act or rules made thereunder, with the intention to evade payment of service tax, the service provider shall be liable to pay penalty in accordance with section 78 of the Finance Act.

Where cenvat credits in respect of input services is wrongly availed or availed in contravention of any of the provisions of these rules, then such person shall be liable to a penalty of an amount not exceeding Rs. 2000/-

Provision for recovery of credits wrongly availed

Where the cenvat credit has been taken or utilized wrongly by the service provider or has been erroneously refunded to him, the same can be recovered from him under Rule 14 of Cenvat Credit Rules 2004. Recovery shall be governed by sections 73 and 75 of Chapter V of Finance Act.

Concept of input service distributor

The term “input service distributor” has been defined by Rule 2(m) of Cenvat Credit Rules 2004 to mean an office of the manufacturer or producer of final products or provider of output service, which receives invoices issued under rule 4A of the Service Tax Rules 1994 towards purchases of input services and issues invoice, bill or, as the case may be, challan for the purposes of distributing the credit of service tax paid on the said services to such manufacturer or producer or provider, as the case may be.

This facility could be used where the manufacturer or service provider has a system of receiving the bills for input services at the Head Office or at branch offices but the credits are to be distributed to the registered service units providing taxable services or the factories engaged in manufacturing. Where the assessee has independent registration for the various service units/factories, this scheme would be particularly useful. The scheme requires the Head Office/branch office seeking to distribute the cenvat credits to the individual units, to register under service tax as an ISD (Input Service Distributor). Once registered, the Head Office/branch office would issue an invoice, bill or a challan to each of the recipient to whom the credit is sought to be distributed. The invoice, bill or challan is to be serially numbered and shall contain –

1. Details as to name, address and registration number of the provider of input services
2. Details of the document/bill given by such input service provider
3. Name and address of the input service distributor
4. Name and address of the recipient of the distributed credit
5. The amount of the credit that is sought to be distributed

The credit amount distributed cannot exceed the amount of service tax paid by the branch office/Head Office. Moreover, the credits pertaining to input services used by the unit engaged exclusively in providing exempted services or manufacturing exempted goods cannot be distributed.

Readers should note that the concept of input service distributor would enable in distributing the credit of service tax on input service whereas what is envisaged u/r 7A is availment of credit of excise duty on inputs and capital goods. The availment u/r 7A would require the office or branch passing on the credit to register as a dealer under central excise and maintain registers recording the movement of materials i.e. receipt from supplier and issue to premises where credits is to be availed as well as the details as to duty per unit paid and duty per unit passed on to the premises where credit is to be availed. A dealer's invoice/bill or challan would have to be raised which would indicate the amount of credit passed on along with the description of goods, value, details of consignor/consignee etc. A quarterly return within 15 days from the end of the quarter would have to be filed by the consigning office/branch/unit.

Pointers for Practice

1. The area of Cenvat credit is an area where cost control is possible as also tax planning. Very often, the assessees have been found to have neglected the Cenvat credits aspect and consequently pay more tax in cash.
2. At times non consideration of the aspects of credit maybe the difference between getting an order or losing one. This is especially true now that the most of the goods are liable to duty of central excise and services for service tax. Therefore the need to avoid breaking the cenvat chain is important.
3. Where ever taxable and exempted services are provided, the segregation of the inputs and input services towards taxable and exempted services has also been found to be inaccurate. This results in many assessees giving up on credits rather than maintaining detailed records and availing the credits that one is entitled to as an assessee.
4. The assessees should also ensure that where ever services are sub-contracted, the sub-contractor charges service tax as the same can be availed as credit provided a proper bill as discussed earlier is available.

5. The definition of input service should be noted carefully as it differs from that of inputs and capital goods in such a way that the service provider can avail credits in respect of services used in relation to setting up, modernization, renovation and repairs of his premises.
6. Where the service provider has substantial service exports, he should make it a point to go in for either refund of credits or rebate of service tax both of which have been explained in a separate chapter. The IT sector could therefore go in for these benefits if exports are substantial.
7. The professional would have to be careful where the assessee opts for provisional determination of credits as any change in value of either goods or services subsequent to 30th of June could lead to a situation where the credits for the year would have to be determined once again. This may happen as a result of any audits being carried out by the department or internally by the management itself.
8. It maybe noted that there is no time limit specified for availment of missed out credits.

CHAPTER 5. VALUATION UNDER SERVICE TAX

Since Service tax is a tax on services which are intangible, valuation of such services for the purpose of charging the tax would assume significance. This is because unlike tangible property in the form of goods which can be compared to other goods in terms of physical attributes and quality, services cannot be compared easily. The service provided by a technician need not be of the same quality as that provided by another technician. Even if they were to be compared, the comparison would be very difficult as the qualities that have to be compared would be intangible. There is also a very significant factor of "what the traffic would bear" in services. Moreover, there could be significant differences between the cost of providing a service and the value that is charged to the client / customer for the same signifying the margins for the service provider. The value of experience may be difficult to estimate.

What is the main basis for valuation?

As per section 67, the amount chargeable to service tax is the gross amount charged for such service provided or to be provided as long as the consideration is wholly in monetary terms. The gross amount charged for the taxable service shall include any amount received towards the taxable service either before, during or after provision of such service.

Where the assessee follows a method of charging one lump-sum amount including service tax, the value determined with the addition of service tax cannot exceed the amount charged by the assessee. For example where the value including service tax @ 10.30 % is Rs. 10 lakhs, the service tax would be determined as follows – ((Rs. 10 lakhs/1.103)*.103) = Rs. 93381.69. The value net of service tax on which such tax is charged = Rs. 1000000 – Rs.93381.69 = Rs. 906618.31 .

“Gross amount charged” as per explanation (c) to section 67, includes payment by cheque, credit card, deduction from account and any form of payment by issue of credit notes or debit notes and book adjustment.

Where the consideration is not wholly in monetary terms, the value would be such that with the addition of service tax would be equivalent to the consideration. The calculation of service tax would be the same as explained in the earlier example.

Where the consideration cannot be determined, the assessee would have to refer the Service Tax (Determination of Value) Rules 2006 in order to ascertain the valuation methodology. As per Rule 3 of the said Rules, the value shall be the gross amount charged by the service provider to provide similar service to any other person in the ordinary course of trade. This proposition would not work and such a price is not possible to be arrived at, but may have to be judicially confirmed in the coming decade.

Where this amount is not available, the equivalent money value of the consideration should be determined and this should not be less than the cost of providing the service. This is possible but may at times be very low as in many services, the actual costs maybe between 1% to 70%. (Too much of subjectivity).

Can the Central Excise Officer question the valuation?

Where the Officer is satisfied that the value has not been determined in accordance with the provisions of this Act or the Rules, he can issue a Show Cause Notice to the assessee to show cause as to why the value should not be as per amount stated in such notice as per Rule 4 of Service Tax (Determination of Value) Rules 2006. The assessee is to be given reasonable opportunity of being heard before the Officer can proceed with the task of determining the value in accordance with the provisions of the Act and the Rules. It is felt that the judicial precedents in regard to valuation of goods under central excise and Customs maybe be useful in defending such valuation disputes and may not end up with any revenue for the Government.

Whether the gross amount charged for the service would include charges reimbursed by the service receiver?

Till 18.04.06, reimbursements were not liable. However, the Service Tax (Determination of Value) Rules 2006 were introduced with effect from 18.04.06. As per Rule 5 of the said Rules, the gross amount charged shall include the cost and expenditure incurred in connection to the taxable services charged to the service receiver. No deduction is allowed for the reimbursement of expenses unless such expenses are incurred by the service provider as a pure agent of the service receiver. The concept of pure agent

requires the service provider to satisfy certain conditions if the reimbursement of expenses is not to suffer service tax.

“Pure agent” as per explanation (1) to Rule 5(2) of Service Tax (Determination of Value) Rules 2006, means a person who –

1. Enters into a contractual agreement with the recipient of service to act as his pure agent to incur expenditure or costs in the course of providing taxable service
2. Neither intends to hold nor holds any title to the goods or services so procured or provided as pure agent of the recipient of service
3. Does not use such goods or services so procured and
4. Receives only the actual amount incurred to procure such goods or services

The conditions to be satisfied in this regard as per Rule 5(2) are as follows –

1. Service provider to act as a pure agent of the recipient of service while making payment to third party for the goods or services procured
2. Service receiver to receive and use the goods or services procured by the service provider on his behalf
3. Service receiver to be liable to make payment to the third party
4. Service receiver to authorise the service provider to make payment on his behalf
5. Service receiver to know that the goods and services, for which payment has been made by the service provider, shall be provided by the third party
6. The payment made by the service provider on behalf of the recipient of service is to be separately indicated in the invoice issued by the service provider to the recipient of service
7. The service provider recovers from the recipient of service only such amount as has been paid by him to the third party
8. The goods or services procured by the service provider from the third party as a pure agent of the recipient of service are in addition to the services he provides on his own account

It is interesting to note that the *vires* of levy of service tax on reimbursements had been questioned by the service provider in Delhi High Court in *Intercontinental Conslt & Technocrats (P) Ltd Vs UOI* (2008 (12) STR 689 (Del)) though the matter is pending adjudication.

Value of materials supplied free of cost by the service receiver

As far as the value of materials supplied free of cost is concerned, authors view is that normally the value of materials so supplied by customer is not to be included in the value of services for charging service tax. This is considering the fact that materials sold during the course of providing service is generally not subject to service tax. The department may however not agree to this view. A decision here would have to be taken on the basis of a review of the agreement entered into between contracting parties in order to see whether the provisions of Section 67(1)(ii) can be invoked i.e pertaining to consideration not being wholly or partly in money. Here, the obligation of the service receiver towards the service provider for the services involved would have to be quantified before one can arrive at a final conclusion. Where the service receiver is obligated to pay certain sum and pays it partly through materials, the same could come under the purview of section 67(1)(ii) and the service provider would be better off including the value of such materials provided by the service receiver in the gross amount for charging service tax, to be on the safer side of law.

Readers may however note that where the taxable service involved comes under the category of works contract service and the service provider opts for the composition scheme for payment of service tax, the gross amount for the contract should include the value of such materials supplied free of cost by the service receiver as well as the value of all services required for the execution of the works contract. This amendment is with effect from 07.07.09 vide Notification 23/2009 ST and does not apply to contracts where the work has commenced or payments made before 07.07.09. The requirement for inclusion of all services needed for execution of works contract could lead to litigation in future especially with regard to those services which are not directly related to the construction process in case of civil works.

Where services are received from abroad and the service receiver is required to pay tax on such import of taxable services, the value should be the actual consideration charged for the service. In the opinion of the authors, where expenses are reimbursed, even such expenses may not form part of the value of the service for the purpose of paying service tax.

It is also to be noted that the rules have overridden the relevant section 67 as they have gone beyond the valuation of services to other amounts received which could be

challenged. However if that is not done then it is preferable to include such amounts unless the pure agent criterion can be met.

Are there any other specific inclusions and exclusions with regard to amount charged for specific services?

Rule 6 provides for certain specific inclusions as well as exclusions with regard to the amount charged for the services. These are given below –

Inclusions in amount charged for service:

1. Commission or brokerage charged by a broker on the sale or purchase of securities (including the commission or brokerage paid by the stock broker to any sub-broker)
2. Adjustments made by the telegraph authority from any deposits made by the subscriber at the time of application for telephone connection or pager or facsimile or telegraph or telex or for leased circuit
3. Amount of premium charged by the insurer from the policy holder
4. Commission received by the air travel agent from the airline
5. Commission, fee or any other sum received by an actuary or intermediary or insurance intermediary or insurance agent from the insurer
6. Re-imbursement received by the authorised service station from the manufacturer for carrying out any service of any motor car, light motor vehicle or two wheeled motor vehicle manufactured by such manufacturer
7. Commission or any amount received by the rail travel agent from the railways or the customer
8. Remuneration or commission by whatever name called, paid to such agent by the client engaging such agent for the services provided by a clearing and forwarding agent to a client rendering services of clearing and forwarding operations in any manner
9. Commission, fee or any other sum by whatever name called paid to such agent by the insurer appointing such agent in relation to insurance auxiliary services provided by an insurance agent

Exclusions with regard to the amount charged:-

1. Initial deposit made by the subscriber at the time of application for telephone connection or pager or facsimile or telegraph or telex or for leased circuit

2. Airfare collected by air travel agent in respect of service provided by him
3. Rail fare collected by rail travel agent in respect of service provided by him
4. Interest on loans

Where during the course of providing service, there is transfer of property in goods, what would be the value?

Where there is transfer of property in goods from the service provider to the service receiver, the service provider would be entitled to a deduction from the gross value to the extent of the value of the goods and materials sold as aforesaid. In other words the service tax is chargeable on the value charged towards labour alone. Where in the invoice the value subjected to VAT is clear, that value can be adopted. Where it is not clear in the invoice the value in the VAT returns can be an indicator. Where no such evidence is available, the actual cost of the goods used for the provision of the service would have to be arrived at and then the gross profit margin added up to arrive at the value of goods sold. This would be in line with the decision in the case of Gannon & Dunkerley ((1958) (9) STC 353 (SC)). Obviously the first option is advisable.

Pointers for practice

- The professional would have to go through the relevant agreements the assessee has with his customers to know the exact amounts being charged and the break ups for the same.
- The professional should be careful enough to ascertain whether the amounts charged are inclusive of all taxes or are the taxes extra. Where the amounts are including taxes and represents amounts charged towards material as well as labour, the gross amount has to be split up in terms of the amounts charged for material and the amounts charged for service. The taxes (VAT on material and service tax on labour portion) can then be calculated using the same inclusive philosophy discussed earlier.
- In case of separate collection of expenditure or costs whether the conditions under Rule 5 (2) are satisfied.

CHAPTER 6. EXEMPTIONS AVAILABLE UNDER SERVICE TAX

Assessees required to pay service tax are often found to be enquiring regarding the availability of exemptions. With the movement towards GST in a few years time and revenue departments looking at ST as the cash cow thanks to the 55% + contribution towards the GDP, the exemptions under service tax are not too many.

However the nature of the levy itself and the fact that there could be instances where during the course of providing services, transfer of property in goods may take place, exemptions have been provided for value of materials sold from payment of service tax. Apart from this, specific exclusions have been made for specified activities within the individual categories liable to tax as taxable services.

Is there an exemption available generally to all service providers exempting value of services up to a certain limit?

Service tax provides for an exemption to small service providers who provide taxable services of a value not exceeding the specified limit. The specified limit is now Rs. 10 lakhs. In other words where the value of taxable services provided do not exceed Rs. 10 lakhs in the previous financial year, the concerned service provider would not be required to pay service tax upto receipts of Rs. 10 lakhs in the current financial year. The exemption is through notification 6/2005 ST dated 01.03.05 as amended from time to time. The service provider should however satisfy certain conditions in order to avail the benefit of this exemption. The conditions to be noted here are as follows –

- Taxable services provided by a person under a brand name or a trade name (whether registered or not) of another person would **NOT** be eligible for this exemption
- A receiver of services who is liable to pay service tax on the services he has received by virtue of section 68(2) cannot avail the benefit of this exemption with regard to such payments. More commonly this is relevant for recipient of GTA Services or in case of import of services where no exemption is available.
- Once an option is exercised in regard to this exemption during a financial year, it cannot be changed in the same financial year. [This however does not mean that the claiming of the exemption makes it compulsory to claim for

the whole year. In between even without reaching Rs.10 lakhs the option to pay can be made.]

- No cenvat credit can be availed on inputs or input services used in providing such output service for which exemption is being claimed.
- Cenvat credit cannot be availed on capital goods received in the premises of provider of such service during the exemption period.
- The service provider shall pay an amount equivalent to the cenvat credit taken by him in respect of inputs lying in stock or in process on the date of availment of exemption. After paying such an amount, if there is any balance of cenvat credit remaining unutilized, such balance would lapse.
- The exemption shall apply in respect of the aggregate value of all taxable services provided by the service provider (even if from more than one premises) and not individually.
- Exempted services shall be outside the purview of the exemption of this notification. In other words, the value for ascertaining the limit of Rs. 10 Lakhs would be that of taxable services alone on which service tax is payable.
- The aggregate value of such services provided in the preceding financial year should not exceed the aforesaid exemption limit.

Is there any exemption from service tax where the service provider transfers property in goods during the course of provision of services?

The service provider who transfers property in goods during the course of providing taxable service would be entitled to avail the benefit of notification 12/2003 ST dated 20.06.03 as amended from time to time. This notification provides a deduction for the value of materials and goods sold by the service provider to the recipient of service, from the gross amount charged for the service. The service provider in effect is required to pay service tax on the balance amount constituting labour charges alone. However, where the service provider avails the benefit of this notification, he cannot avail cenvat credit of the excise duty paid on goods and materials so sold but can avail credit of service tax paid on input services. Even excise duties incurred on capital goods can be availed as credits. One big advantage of this notification is that the same is not restricted to any one single category of service. Thus where the service provider knows the amounts being charged for labour and the amounts towards sale of goods or materials, this notification can be followed.

Is there any other exemption available which can also be used in a scenario where the value of materials/goods sold cannot be quantified or ascertained separately?

Apart from 12/2003 ST, there is another notification applicable to specified service providers. The service providers to whom the notification would apply are mentioned in the notification itself. The concerned notification is 1/2006 ST dated 01.03.06 as amended from time to time. Notification 1/2006 provides for a fixed deduction from the gross amount charged for the service subject to conditions specified being satisfied. The service provider opting for this notification cannot avail cenvat credits at all plus he would also not be entitled to avail the benefit of exemption under notification 12/2003 ST. The specified categories as well as the exemptions available are given in the table below:

<i>Service category</i>	<i>Exemption as a percentage of gross amount charged</i>	<i>Remarks if any</i>
Mandap keeper's service - in relation to use of mandap. It includes services provided by a hotel as mandap keeper	40%	The mandap keeper should also provide catering services i.e. supply of food and the charges for the same should be included in the gross amount and indicated on the invoice
Services provided or to be provided by a tour operator to any person in relation to a package tour.	75%	The bill for the tour should include the charges for travel, transportation, accommodation, guide and food, entry to monuments and other similar facilities extended.
Services provided by a tour operator in relation to booking or arranging of accommodation in relation to a tour	90%	The charges on the bill should also include the cost/charges for such accommodation and not just the service charges.
Services other than the ones specified above provided by a tour operator in relation to a tour	60%	The amount charged on the bill should be the gross amount charged for the services in relation to the tour.

Rent-a-cab scheme operator in relation to renting of cabs	60%	
Holding of a convention where catering service is also involved	40%	The amount on the bill should also include the charges for such catering.
Business auxiliary service in relation to production or processing of parts and accessories used in the manufacture of cycles, cycle rickshaw, hand operated sewing machines for or on behalf of client	30%	Gross amount charged should include cost of inputs and input services whether or not supplied by the client.
Erection, commissioning or installation of plant, machinery, equipment or structures under a contract	67%	The gross amount charged shall include the value of such plant, machinery, equipment, structures and other parts sold. Moreover this exemption is at the option of the service provider
Commercial or industrial construction service	67%	The gross amount shall include the value of goods and materials supplied or provided or even used by the service provider for providing such service. This exemption shall not be available in case of completion and finishing services in relation to building or civil structure.
Outdoor caterer – services in relation to catering	50%	The amount charged should include the value of food supplied as well.
Services by a pandal or shamiana contractor in relation to a pandal or shamiana including services	30%	The gross amount for the service should also include the charges towards catering services

as a caterer		
Construction of complex	67%	The gross amount shall include the value of goods and materials supplied or provided or even used by the service provider for providing such service. This exemption shall not be available in case of completion and finishing services in relation to residential complex.
Transport of goods in containers by rail	70%	

“Food” here means a substantial and satisfying meal.

Exemption to contract carriage permit holders

Notification 20/2009 ST dated 07.07.09 provides exemption on taxable services falling under heading tour operator's services for inter state or intra state transport of passengers (excluding tourism, conducted tours, charter on hire services) provided or to be provided to any person by a tour operator having a contract carriage permit, from service tax.

Exemption on Goods Transport Agency service

Notification 13/2008 ST dated 01.03.2008 provides an exemption of 75% of the gross amount charged towards taxable service in relation to transport of goods by road. In other words, service tax is to be charged on 25% of the gross amount charged towards freight.

Services provided to a developer of Special Economic Zone or a Unit of a Special Economic Zone

The position regarding exemption on taxable services provided to SEZ unit or developer has undergone change. The notification 4/2004 ST dated 31.03.2004 which provided an exemption on such taxable services was rescinded when Notification 9/2009 ST dated 03.03.09 was introduced. This Notification was later amended by Notification 15/2009 ST dated 20.05.09.

The SEZ unit or developer receiving such taxable service would now be required to go in for refund of the service tax paid unless the services received for authorized operations in the Zone are consumed wholly within the said Zone. Where the services are to be consumed wholly within the SEZ, no service tax would be payable. Where the services are not for consumption wholly within the Zone, the SEZ unit or developer would have to examine the refund route as laid down in the Notification 9/2009 ST. The services would have to be provided in relation to operations which are authorised in the SEZ and received by the SEZ developer /unit. But one saving grace is that the service may be provided even outside the said SEZ as long as the receiver is the SEZ developer or unit, for the purpose of going in for refund. In other words, place of performance of the taxable service would not be the factor determining the service tax refund. The following aspects would be relevant:

- The service provider providing the taxable service to SEZ unit or developer in relation to authorised operations in the SEZ (but not consumed wholly within the SEZ) would be required to pay service tax and cannot go in for exemption. As far as the service providers are concerned this is a blessing in disguise as they do not have to dispute the same.
- The list of services required for authorised operations would have to be approved by the Approval Committee and the SEZ unit/developer would have to obtain this approval.
- The SEZ developer or unit would have to use the specified services in relation to authorised operations in the SEZ.
- The SEZ developer or unit would have to pay service tax on the specified services to the service provider.
- Cenvat Credit of service tax paid on such specified services cannot be taken by the SEZ developer or unit under Cenvat Credit Rules 2004.
- No exemption or refund of service tax paid on such specified services can be claimed under any other notification.
- Where the SEZ developer or unit happens to be liable under Section 68(2) as a receiver of taxable service, exemption can be claimed from payment of such service tax by the concerned SEZ developer or unit.
- A refund claim would have to be filed by the SEZ developer or unit with the jurisdictional ACCE / DCCE within six months (or extended time) from the date of

actual payment of service tax. (The procedures are given in the Chapter on Refunds and Rebates).

Certain other specific exemptions –

Exemption to service provided by Technology Business Incubators or Science and Technology Entrepreneurship Parks

Exemption from service tax has been provided to all taxable services provided by Technology Business Incubators (TBI)/ Science and Technology Entrepreneurship Parks (STEP) recognised by National Science and Technology Entrepreneurship Board of the Department of Science and Technology under notification 9/2007 ST dated 01.03.2007. The incubator availing exemption is required to follow the procedures set out in the said notification. They are also required to furnish the details of incubatees to be obtained from each such incubatee to whom they are providing assistance.

Exemption from service tax is also available to taxable services up to Rs. 50 lakhs in a financial year provided by each incubatee entrepreneur who is located within the premises of an incubator where the total business turnover of the incubatee entrepreneur does not exceed Rs. 50 lakh in a financial year/ preceding financial year. Exemption is available for three years effective from the date of signing an agreement with the incubator vide notification 10/2007 ST dated 01.03.2007.

Exemption to cargo handling services relating to agricultural produce

Cargo handling services relating to agricultural produce or goods intended to be stored in a cold storage are exempt from service tax under notification 10/2002 ST dated 01.08.2002

Exemption to consulting engineer when cess is paid under Section 3 of Research and Development Cess Act 1986

The consulting engineer is entitled to exemption in terms of service tax on taxable services provided on transfer of technology, to the extent of cess paid on transfer of technology under Notification 18/2002 ST dated 16.12.2002

Exemption to commission agent

The business auxiliary service provided by a commission agent in relation to sale or purchase of agricultural produce is exempt from service tax under notification 13/2003 ST dated 20.06.03

Exemption to mandap keeper

Under Notification 14/2003 ST dated 20.06.2003, a mandap keeper is exempted from service tax on taxable services provided for use of precincts of a religious place as a mandap.

Exemption to mechanised slaughter house

Taxable services provided by a mechanised slaughter house in relation to slaughtering of bovine animals has been exempted from service tax under Notification 2/2000 ST dated 01.03.2000

Exemption to services in relation to collection of duties and taxes of the Central or State governments

Notification 13/2004 ST dated 10.09.2004 exempts taxable services in relation to collection of duties and taxes levied by central and state governments and provided to them by a banking company or NBFC or Financial institutions or body corporate, from the payment of service tax.

Exemption on interest charged by banking company, NBFC, body corporate or Financial Institutions or any other person.

Notification 29/2004 ST dated 22.09.2004 exempts the interest amount charged on overdrafts, cash credits, discounting of bills, bills of exchange or cheques, from service tax. The interest should be shown separately on the invoice or the bill.

Exemption with regard to technical and clinical testing

With effect from 01.03.2007, exemption from service tax is being provided to technical testing and analysis services provided in relation to testing of newly developed drugs including vaccines and herbal remedies on human participants by a clinical research organisation approved to conduct clinical trials by the Drugs Controller General of India vide notification 11/2007 ST dated 01.03.2007

Exemption on technical inspection, certification, technical testing and analysis service

Notification 6/2006 ST dated 01.03.2006 provides exemption from service tax on taxable services of technical testing and analysis of water quality provided or to be provided to any person by a government owned state or district level laboratory.

Exemption to a practising chartered account, practising cost accountant and a practising company secretary

Notification 25/2006 ST dated 13.07.2006 provides exemption from service tax in respect of taxable services in relation to representation of the client before any statutory authority under any proceeding of law initiated by way of issue of notice.

Exemption on service provided by a person having his place of residence outside India

Notification 14/2008 ST dated 01.03.2008 provides an exemption from service tax on taxable service provided by a person resident outside India and received by a hotel in India in relation to booking of accommodation in the said hotel for a person resident outside India. Readers may refer the said notification for the manner of determination of residential status of the service provider and service receiver. This would have significance for the service receiver as generally he is liable to tax on receipt of taxable services from abroad.

Exemption in respect of services by Resident Welfare Associations

Exemption from service tax is available to services provided by Resident Welfare Associations to their members where the monthly contribution of a member does not exceed Rs.3000/- per month vide notification 8/2007 ST dated 01.03.2007

Exemption in respect of Digital Cinema Service

Exemption from service tax is available with regard to services provided by the digital cinema service provider to the producer or distributor in relation to the delivery of content of cinema in digital form after encryption electronically to a cinema theatre for exhibition through the use of satellite, microwave or terrestrial communication line and not by any physical means including CD or DVD, as per notification 12/2007 ST dated 01.03.2007.

Exemption to Services provided to United nations or an International Organization declared by the government

Taxable services provided by any person to the UN or an International Organisation are exempt from the whole of service tax with effect from 02.08.2002 vide notification 16/2002 ST dated 02.08.2002. The international organisation must be declared by the Central Government in pursuance of section 3 of the United Nations (Privileges and Immunities Act 1947) to which the provisions of the Schedule to the said Act apply.

Exemption on business auxiliary service

Notification 14/2004 ST dated 10.09.2004 provides exemption to the following taxable services under category BAS provided in relation to agriculture, printing, textile processing and education from service tax. The taxable services enjoying exemption are-

- Production or processing of goods for or on behalf of the client
- Provision of service on behalf of the client
- Procurement of goods or services which are inputs for the client
- Any service which is incidental or auxiliary to the above mentioned services.

Exemption on business auxiliary service- production or processing of goods for or on behalf of client

Notification 8/2005 ST dated 01.03.2005 exempts taxable service in relation to production or processing of goods for or on behalf of client where the processing is on raw materials or semi finished goods supplied by client and the processed goods are sent back to the client for use in further manufacturing of dutiable goods at his end and clearance on payment of duty.

Exemption in respect of intellectual property service

Notification 17/2004 ST dated 10.09.2004 provides an exemption from service tax on taxable services (intellectual property service) provided by a holder of intellectual property right to the extent of cess paid under R&D Cess Act 1986 towards import of technology.

Exemption to services provided by or to the Reserve Bank of India

The following services have been exempted from service tax vide notification 22/2006 ST dated 31.05.06 -

- Taxable services provided or to be provided to any person, by the RBI

- Taxable services provided or to be provided by any person, to the RBI when the service tax for such services is liable to be paid by RBI u/s 68(2) of Chapter 5 of Finance act read with Rule 2 of Service Tax Rules 1994
- Taxable services received in India from outside India by the RBI u/s 66A of the Finance Act 1994

Exemption on services provided in relation to inter bank sale or purchase of foreign currency

The services falling under the categories of Banking and other financial services or foreign exchange broker's services in relation to inter bank sale or purchase of foreign currency provided by one scheduled bank to another has been exempted from service tax by notification 19/2009 ST dated 07.07.09

Exemption in respect of services by a service provider providing general insurance business in relation to insurance of sheep

The taxable services provided by an insurer carrying on general insurance business, to a policy holder in relation to insurance of sheep has been exempted from service tax till 31.12.2009 under Notification 31/2006 ST dated 11.12.2006

Exemption to Goods Transport Agency

Notification 33/2004 ST dated 03.12.2004 provides exemption from service tax to taxable services in relation to transport of fruits, eggs, vegetables, or milk by road in a goods carriage.

Exemption to Goods Transport Agency u/n 34/2004 ST dated 03.12.2004

This notification exempts taxable service in relation to transport of goods by road in a goods carriage from payment of service tax where in case of individual consignments, the gross amount charged for the service does not exceed Rs. 750 and in other cases, the gross amount does not exceed Rs. 1500.

Exemption on certain specified taxable services provided to a GTA

Notification 1/2009 ST dated 05.01.2009 provides exemption from service tax to certain specified taxable services provided to a Goods Transport Agency for use in relation to transport of goods by road service provided by the GTA to its customer.

The specified taxable services are –

- Clearing and forwarding agent's services
- Cargo handling agency service
- Manpower recruitment service
- Storage and warehousing service
- Business auxiliary service
- Packaging service
- Support service of business or commerce
- Supply of tangible goods service

This notification is now given retrospective effect from 01.01.05.

Exemption in relation to financial leasing services

Notification 4/2006 ST dated 01.03.06 provides an exemption in respect of financial leasing services including equipment leasing and hire purchase taxable under the head banking and other financial services. The exemption is on 90% of the interest amount i.e difference between the installment amount paid towards repayment of the lease amount and the principal amount contained in such installment. The exemption is on interest component alone and not on other charges like lease management fee, processing fee, documentation charges or administration fee.

Exemption on certain services received by exporter of goods

Notification 18/2009 ST dated 07.07.09 provides exemption from service tax on services of transportation of goods by road in a goods carriage to port or airport for export of goods as well as services of commission agent engaged by the exporter outside India (falling under category of Business Auxiliary Service) for promoting the sale of goods. The exemption on commission is limited to 1% of free on board value of export goods for which the said services is used.

Exemption from service tax on services provided to members

Notification 16/2009 ST dated 07.07.09 provides exemption from service tax on services provided falling under heading club and association service by specified associations engaged in export promotion, to its members. The list of associations covered has been provided in the concerned notification.

Exemption to insurer carrying General Insurance Business under Universal Health insurance scheme

Taxable service that is provided by an insurer carrying on general insurance business, to a policy holder in relation to General Insurance Business provided under the Universal Health Insurance Scheme, is exempted from service tax under notification 16/2003 ST dated 11.07.03

Exemption in relation to commercial training or coaching centre

Notification 10/2003 ST dated 20.06.03 exempts taxable services provided by a commercial training or coaching centre in relation to commercial training or coaching forming an essential part of the curriculum or course of any other establishment or institute leading to issuance of certificate, diploma, degree or educational qualification recognised by law, from the whole of service tax unless the charges for such services are paid directly by the person undergoing training, to such commercial training or coaching centre. If paid directly, the services would be liable to service tax.

Exemption to commercial training or coaching by a vocational or recreational training institute

Notification 24/2004 ST dated 10.09.2004 provides exemption from service tax in relation to taxable services in relation to commercial training or coaching provided by a vocational training institute or a recreational training institute. (The former does not include a computer training institute).

Exemption to exporters of selected goods on services obtained by them in relation to exhibition of their goods

Notification 43/2007 ST dated 29.11.07 exempts taxable service in relation to business exhibition provided by the organiser of business exhibition to a manufacturer of goods falling under chapter 57, 61, 62 and 63. The goods would have to be exported in order to avail benefit of this exemption. The exemption shall be in accordance with the guidelines and the procedures given in the said notification. The manufacturer should first of all pay the service tax and then go for a claim for refund on the same on export. This notification was valid till 31.03.2009 and one would have to see whether the benefit of exemption would be extended beyond this date.

Exemption on services provided to diplomatic agents, family members of such agents and career consular officers posted in foreign diplomatic mission or consular post in India

This would be available as per notification 34/2007 ST dated 23.05.07 where the services are for their personal use. The conditions prescribed in the notification are to be followed to secure the exemption. Where it is for the official use of the mission or consular post, the same would be exempt u/n 33/2007 ST dated 23.05.07

Pointers for practice

- The professional should ensure that where benefits of exemptions are claimed, the conditions prescribed for the same are complied with, failing which the benefit could be denied.
- The professional should also weigh the benefits of all the concerned alternatives before suggesting the exemption to be claimed where he acts in an advisory capacity. The availment of exemptions generally limits/ bars the whole or part of availment of cenvat credits.
- The professional should also confirm that the assessee is really entitled to claim the benefit of exemption and this should be ascertained on a review of the records of the assessee. Where services are wrongly classified, or the values incorrectly determined under service tax, it could have a huge impact on availability of exemptions and service tax liability.

CHAPTER 7. IMPORT AND EXPORT OF SERVICES

Service tax is payable on taxable services provided by a service provider within the country. Now, an assessee in India may also provide taxable services to a service receiver abroad. Export of services is also not taxed just like export of goods. However, the criterion for determining whether services are exported or not cannot be the same as for goods as services are intangible and different from goods. Keeping this in mind the government has framed the Export of Service Rules 2005 to determine whether services are exported or not.

Another feature which stands out in service tax is the taxing of taxable services received in the hands of the service receiver. We have seen earlier that certain categories of services are taxed in the hands of the service receiver where they are received from a service provider within the country. In addition to this, where taxable services are received in India from a service provider outside the country, the same can be taxed in the hands of the service receiver within the country under reverse charge mechanism. The criterion for finding out whether a service is taxable in this regard in the hands of the service receiver or not, has been laid out in the Taxation of Services (Provided from Outside India and Received in India) Rules 2006

It is to be noted that services provided and received outside India would not be the subject matter of the levy itself as this tax is a destination based tax as held in the All India Tax Practitioners decision of the Supreme Court ((2007) (07) STR 625)

When is a service said to have been imported into the country for the purpose of taxing the same in the hands of the service receiver?

The charging section which seeks to tax services received in India from abroad is section 66A. In order to tax the service concerned, it should first of all be a taxable service. Where the taxable service covered u/s 65(105) is -

- Provided or to be provided by a person who has established a business or has a fixed establishment from which the service is provided or to be provided or has his permanent address or usual place of residence, in a country other than India, and

- Received by a person (hereafter referred to as the recipient) who has his place of business, fixed establishment, permanent address or usual place of residence, in India,

Then, such taxable service shall be treated as if the recipient had himself provided the service in India unless such recipient is an individual and the service is received for purposes other than for use in any business or commerce.

Where the service provider has his business establishment both in that country as well as in some other country, the country where the establishment concerned directly with the provision of service is located, shall be treated as the country from where the service is provided or to be provided.

What would be the position where an entity has establishments in India as well as abroad and the entity abroad provides services to the Indian unit?

Where a person is carrying on a business through a permanent establishment in India and through another permanent establishment in a country other than India, such permanent establishments shall be treated as separate persons for the purposes of this section. In other words, where the establishment abroad provides services finding a mention in section 65(105), to the establishment in India, then such services would be taxed in the hands of the Indian establishment as per the Taxation of Services (Provided from Outside India and Received in India) Rules 2006. It is worthwhile to note that the concept of establishment has not been defined or clarified under service tax and one would have to refer the dictionary meaning of the term establishment.

As per the meaning given by Webster's Unabridged Dictionary, establishment means a place of business together with its employees, merchandise, equipment etc.

The definition u/s 66A (2) contains an explanation as to the cases where there would be deemed to be a business establishment. As per explanation 1 to section 66A (2), where a person carries on a business through a branch or agency in any country, he shall be treated as having a business establishment in that country. Thus even where a branch office say in London provides taxable services to Head Office in Mumbai, the Head Office would have to consider its liability in accordance with the stated Rules though this concept does not seem very sound.

Explanation 2 to section 66A (2), clarifies the concept of usual place of residence in relation to a body corporate to mean the place where it is incorporated or otherwise legally constituted.

It is interesting to note here that there has been considerable confusion in the past regarding the taxability of services received from abroad and the confusion to a certain extent had arisen due to the amendment to Rule 2 of Service Tax Rules 1994 with effect from 16.08.02. The amendment was in terms of Rule 2(1)(d)(iv) seeking to treat the service receiver in India as the person liable to pay tax where the service provider was a non-resident not having an office in India. However, the tax liability on the service receiver could not be fastened as the amendment in the Rules was held to be not sufficient for introducing a liability in the absence of anything specific in the statute as laid down in *Hindustan Zinc Ltd. Vs CCE Jaipur* (2008 (11) STR 338 (Tri-LB)). Moreover, departmental Circular 36/04/ 2001-CX (ST) dated 08.10.01 had clarified that service provided beyond the territorial waters of India was not liable to tax keeping in mind the spirit of Section 64. This Circular was withdrawn on 10.05.07 after introduction of Section 66A in Chapter V of Finance Act 1994 as amended from time to time.

Readers can note that the Bombay High Court in *Indian National Ship Owners vs UOI* (2009 (13) STR 235(Bom)) had allowed a writ petition challenging the levy of service tax on taxable services received from abroad before 18.04.2006. Therefore where a taxable service is provided from outside India and received by a service receiver in India, the liability for such service would only be from 18.04.2006. This in the authors' view would have to be distinguished from a scenario where a person having his permanent establishment outside India, provides a taxable service in India to the service receiver having his office or permanent establishment in India. In this case, the liability in the hands of the service receiver would exist even for taxable services received before 18.04.06. Readers should note the distinction between the two cases covered here as it boils down to the place of performance of taxable service in respect of taxable services received prior to 18.04.06.

With effect from 18.04.2006, the question whether a taxable service is received in India at all or performed in India or outside would have to be answered after going through the provisions of Taxation of Services (Provided From Outside India and Received in India) Rules 2006.

What do the Taxation of Services (Provided from outside India and Received in India) Rules 2006 say?

Rule 3 of the said rules basically talks about the basis for treating the taxable services as having been received in the country from abroad. It is worthwhile to note here that the criterion for determining this is not the same for all the taxable services and that the various taxable services have been divided into three basic categories for the purpose.

- The first category deals with the taxable services received in relation to an immovable property. With regard to this category, the taxable services provided or to be provided in relation to an immovable property situated in India shall be regarded as having been received in India. In other words the **location of the immovable property** would be the critical factor. Where it is outside India, the taxable service provided in relation to such property would not be liable in the hands of the receiver.
- The second category deals with taxable services with regard to which the place of **performance** would be the critical factor. Here, the taxable services shall be regarded as having been received in India if such services have been performed in India. Performance here could even be part performance in India.
- The third category deals with taxable services with regard to which the **location of the recipient** himself would be the critical factor. Here, the taxable services shall be regarded as having been received in India if such services have been received by a recipient located in India for use in relation to business or commerce.

It is pertinent to note here that third category would not include the following taxable services:

- Services by an aircraft operator in relation to scheduled or non-scheduled air transport of passengers embarking in India for international journey u/s 65(105)(zzzo)
- Services in relation to transport of persons by a cruise ship, embarking from any port or other port in India u/s 65(105)(zzzv)

The third category would specifically cover the following taxable services where they are not provided in relation to an immovable property -

- General Insurance business service provided by an insurer under section 65(105)(d)

- Survey and map making services u/s 65(105)(zzzc) by a person other than an agency under control of or authorized by the Government,
- Auction of property (whether movable or immovable or tangible or intangible) other than by government or under directions or orders of Court, u/s 65(105)(zzzr)

Note: - It is important to note that the third category requires the services to be for use in relation to business or commerce. Where they are for personal use of the assessee, the same would not be liable under the third category. This clause is not applicable to the earlier two categories. The service receiver liable to pay service tax here would have to get himself registered under Service Tax as per Rule 4 of the said rules. Moreover, for the purpose of payment of such service tax, cenvat credits cannot be utilized as the services would not be considered as output services in the hands of the service provider. But he can avail cenvat credits of the service tax paid on such services once the payment has been made, and this could even be on the basis of the challan through which the payment would have been made earlier, as per Rule 9(1)(e) of Cenvat Credit Rules 2004.

Where the services of management, maintenance or repair or technical testing and analysis or technical inspection and certification falling under clauses (zzg), (zzh) and (zzi) of section 65(105) are provided remotely through internet or an electronic network in relation to any goods or material or any immovable property situated in India at the time of provision of service, such services shall be treated as having been performed in India.

In respect of supply of tangible goods service falling under clause 65(105)(zzzzj), the service would be regarded as having been received by a recipient located in India if the tangible goods are located in India during the period of their use by the recipient.

Note: - With effect from 07.07.09, taxable services received in installations, structures and vessels in Continental Shelf of India as well as the Exclusive Economic Zone from abroad, would also be regarded as import of services. This is a result of amendment brought about in the aforesaid Rules by Notification 22/2009 ST dated 07.07.09

Provisions in case of export of services

Power of the government to frame rules or to grant exemption or rebate

The Central Government is empowered under section 93 to grant exemption from service tax and the exemption may be whole or partial and may be subject to conditions which may be specified. The Government is also empowered to frame Rules u/s 94 for carrying out the various provisions of Chapter V. The Rules which can be framed by the Government with regard to exports may provide for -

- Determination of export of taxable services
- Exemption to or granting rebate of service tax paid on taxable services exported out of India
- Rebate of service tax paid or payable on the taxable services which have been consumed for or duties paid or deemed to have been paid on goods used for providing taxable services which are exported out of India
- Rebate of service tax paid or payable on the taxable services used as input services in the manufacturing or processing of goods exported out of India u/s 93A.

When would a service provided to a service receiver located outside India be regarded as having been exported?

The service that is provided should be provided in accordance with the requirements of Rule 3 of Export of Service Rules 2005 which have been framed in this regard. An interpretation of this rule would indicate that the following conditions would have to be satisfied in order to treat a taxable service as having been exported –

1. Such service is provided from India and used outside India
2. Payment for such service provided outside India is received by the service provider in convertible foreign exchange
3. The additional criterion depending on the category of service involved would have to be satisfied. This requirement is explained below -

For the purpose of meeting this additional criterion, the rule has basically divided the taxable services into three categories for the purpose of determining whether a taxable service is exported or not.

- The first category deals with the taxable services received in relation to an immovable property. With regard to this category, the taxable services provided or to be provided in relation to an immovable property situated outside India shall be regarded as having been exported from India. In other words the location of the immovable property would be the critical factor.
- The second category deals with taxable services with regard to which the place of performance would be the critical factor. Here, the taxable services shall be regarded as having been exported from India if such services have been performed outside India. Performance here could even be part performance outside India.
- The third category deals with taxable services with regard to which the location of the recipient himself would be the critical factor. Here, the taxable services when provided in relation to business or commerce shall be regarded as having been exported from India if such services have been provided to a recipient located outside India. When not provided in relation to business or commerce, the taxable service shall be regarded as having been exported if the service receiver is outside India at the time of provision of such service.

It is pertinent to once again note here that the third category (recipient based) would not include the following taxable services –

- Services by an aircraft operator in relation to scheduled or non-scheduled air transport of passengers embarking in India for international journey u/s 65(105)(zzzo)
- Services in relation to transport of persons by a cruise ship, embarking from any port or other port in India u/s 65(105)(zzzv)

The third category would specifically cover the taxable services where they are not provided in relation to an immovable property. This would be the same as explained under import of services.

Where the recipient has a commercial establishment or any office relating thereto in India, such taxable services provided shall be treated as export of service only when

order for provision of such service is made from any of his commercial establishments or offices located outside India.

“India” includes the designated areas in the continental shelf and exclusive economic zone of India as declared by the notifications of the Ministry of External Affairs, Government of India.

Where the services of management, maintenance or repair or technical testing and analysis or technical inspection and certification falling under clauses (zzg), (zzh) and (zzi) of section 65(105) are provided remotely through internet or an electronic network in relation to any goods or material or any immovable property situated outside India at the time of provision of service, such services shall be treated as having been performed outside India and treated as export of service.

In respect of supply of tangible goods service falling under clause 65(105)(zzzzj), the service would be regarded as having been exported outside India if the tangible goods are located outside India during the period of their use by the recipient abroad.

No payment of service tax in case of export of service

A taxable service can be exported without payment of service tax by virtue of Rule 4 of Export of Service Rules 2005. Moreover, Rule 5 also provides the facility for the government to grant rebate by a notification through which rebate of service tax paid (if any) on such taxable service or service tax or duty paid on input services or inputs used in providing such taxable service can be allowed subject to conditions prescribed being met.

Grouping of the services

First category services – Taxable services provided in relation to immovable property

- General Insurance business provided by an insurer under section 65(105)(d)
- Architectural service u/s 65(105)(p)
- Interior decorator's service u/s 65(105)(q)
- Real estate agent's service u/s 65(105)(v)
- Commercial or industrial construction service u/s 65(105)(zzq)

- Site formation, clearance, excavation and earthmoving and demolition services u/s 65(105)(zzza)
- Dredging services u/s 65(105)(zzzb)
- Survey and map making services u/s 65(105)(zzzc)
- Construction of complexes u/s 65(105)(zzzh)
- Auction of property u/s 65(105)(zzzr)
- Mining of mineral, oil and gas 65(105)(zzzy)
- Renting of immovable property 65(105)(zzzz)
- Works contract service 65(105)(zzzza)

Second category services – Taxable services with regard to which place of performance is the key

- Services by a stock broker in connection with sale or purchase of listed securities u/s 65(105)(a)
- Services by a courier agency in relation to door to door transportation of time sensitive documents, goods or articles u/s 65(105)(f)
- Services by a customs house agent in relation to entry or departure of conveyances or the import or export of goods u/s 65(105)(h)
- Services by a steamer agent in relation to a ship's husbandry or dispatch or any administrative work related thereto as well as the booking, advertising, canvassing of cargo u/s 65(105)(i)
- Clearing and forwarding agent's services u/s 65(105)(j)
- Air travel agent's services u/s 65(105)(l)
- Services by a mandap keeper (including catering) u/s 65(105)(m)
- Tour operator's services u/s 65(105)(n)
- Services by a rent-a-cab-scheme operator u/s 65(105)(o)
- Services by a practising chartered accountant u/s 65(105)(s)
- Services by a practising cost accountant u/s 65(105)(t)
- Services by a practising company secretary u/s 65(105)(u)
- Security agency's services u/s 65(105)(w)
- Credit rating agency's services u/s 65(105)(x)
- Market research agency's services u/s 65(105)(y)
- Underwriter's services u/s 65(105)(z)

- Photography studio or agency's services u/s 65(105)(zb)
- Services in relation to holding of a convention u/s 65(105)(zc)
- Services by a video production agency in relation to video-tape production u/s 65(105)(zi)
- Sound recording studio or agency's services u/s 65(105)(zj)
- Port services by any person u/s 65(105)(zn)
- Services by an authorised service station in relation to service of motor vehicles u/s 65(105)(zo)
- Beauty parlour's services in relation to beauty treatment u/s 65(105)(zq)
- Cargo handling agency's services u/s 65(105)(zr)
- Dry cleaning services by a dry cleaner u/s 65(105)(zt)
- Event manager's services in relation to event management u/s 65(105)(zu)
- Fashion designer's services u/s 65(105)(zv)
- Health club and fitness centre's services in relation to health and fitness u/s 65(105)(zw)
- Services by a storage or warehouse keeper in relation to storage and warehousing of goods u/s 65(105)(zza)
- Services in relation to commercial training or coaching by a commercial training or coaching centre u/s 65(105)(zzc)
- Services in relation to erection, commissioning or installation by a commissioning and installation agency u/s 65(105)(zzd)
- Services in relation to access of internet by an internet cafe u/s 65(105)(zzf)
- Services in relation to management, maintenance or repair u/s 65(105)(zzg) *(refer para on amendment given earlier)*
- Services in relation to technical testing and analysis by a technical testing and analysis agency u/s 65(105)(zzh) *(refer para on amendment given earlier)*
- Services in relation to technical inspection and certification by a technical inspection and certification agency u/s 65(105)(zzi) *(refer para on amendment given earlier)*
- Port services by other port or person authorised u/s 65(105)(zli)
- Services by airports authority or person authorised by it in an airport or a civil enclave u/s 65(105)(zzm)

- Services by an aircraft operator in relation to transport of goods by aircraft u/s 65(105)(zzn)
- Services in relation to business exhibition by the organiser of a business exhibition u/s 65(105)(zzo)
- Services in relation to transport of goods by road in a goods carriage by a goods transport agency u/s 65(105)(zzp)
- Services in relation to opinion poll by an opinion poll agency u/s 65(105)(zzs)
- Services by an outdoor caterer u/s 65(105)(zzt)
- Services in relation to survey and exploration of minerals u/s 65(105)(zzv)
- Services by a pandal and shamiana contractor (including catering) u/s 65(105)(zzw)
- Travel agent's services u/s 65(105)(zzx)
- Services in relation to forward contract by a member of a recognised association or a registered association u/s 65(105)(zzy)
- Services in relation to cleaning activity u/s 65(105)(zzzd)
- Provision of services or facilities or advantages by a club or association to its members for a subscription or any other amount u/s 65(105)(zzze)
- Services in relation to packaging activity u/s 65(105)(zzzf)
- Services in relation to transport of goods in containers by rail in any manner other than Government railways u/s 65(105)(zzzp)
- Stock exchange service 65(105)(zzzzg)
- Services in relation to trading, processing, clearing and settlement of transactions in goods or forward contracts 65(105)(zzzzh)
- Clearing house service 65(105)(zzzzi)

Third category – Taxable services where the location of the recipient would hold good

The services not covered in the aforesaid two categories would be covered here unless there is exclusion with regard to the concerned taxable service under this category as explained earlier. The services covered here consequently would be –

- General insurance business service not for immovable property 65(105)(d)
- Advertising service 65(105)(e)
- Consulting engineer 65(105)(g)

- Manpower recruitment 65(105)(k)
- Management consultant 65(105)(r)
- Scientific or technical consultancy 65(105)(za)
- Online information and database access or retrieval 65(105)(zh)
- Broadcasting services 65(105)(zk)
- Insurance auxiliary service pertaining to general insurance business 65(105)(zl)
- Banking and other financial services 65(105)(zm)
- Cable operator services 65(105)(zs)
- Life insurance business services 65(105)(zx)
- Insurance auxiliary service pertaining to life insurance business 65(105)(zy)
- Rail travel agent 65(105)(zz)
- Business auxiliary service 65(105)(zzb)
- Franchisee services 65(105)(zze)
- Foreign Exchange Broker 65(105)(zzk)
- Intellectual property service 65(105)(zzr)
- TV or radio program services 65(105)(zzu)
- Transport of goods through pipeline 65(105)(zzz)
- Survey and map making not for immovable property 65(105)(zzzc)
- Mail list compilation 65(105)(zzzg)
- Registrar to an issue 65(105)(zzzi)
- Share transfer agent 65(105)(zzzj)
- ATM operations, maintenance or management 65(105)(zzzk)
- Recovery agent 65(105)(zzzl)
- Sale or time or space services 65(105)(zzzm)
- Sponsorship service 65(105)(zzzn)
- Support service of business or commerce 65(105)(zzzq)
- Auctioneer's service not for immovable property 65(105)(zzzr)
- Public relations services 65(105)(zzzs)
- Ship management services 65(105)(zzzt)
- Credit card, debit card related services 65(105)(zzzw)
- Telecommunications services 65(105)(zzzx)
- Development and supply of content services 65(105)(zzzzb)

- Asset management services 65(105)(zzzzc)
- Design services 65(105)(zzzzd)
- Internet telecommunication services 65(105)(zzzu)

- Information technology software services 65(105)(zzzze)
- Services in relation to management of investment (ULIP) 65(105)(zzzzf)
- Services in relation to supply of tangible goods 65(105)(zzzzj)

Pointers for practice

- The professional should go through the various agreements the client has with his customers to understand the terms and conditions as to the status as to Import or Export.
- The billing and sales correspondences can also indicate the real nature of the transaction. It has been observed that at times the explanation, billing as well as the agreement are surprisingly all different.
- The professional is also advised to exercise due care in cases where the performance based criterion applies in order to determine the status as to Import or Export of service as often the cost of non-compliance could be high.
- The criterion for specified service provider, specified service receiver is as relevant as the specified service for the attraction of the levy where received from a non resident.
- The professional should also ensure that the client claims the benefits associated with export of services mainly in the form of refunds, rebates etc.

CHAPTER 8. REFUNDS AND REBATES

The discussion on refunds should be taken up only after examining certain provisions of Central Excise Act 1944 which are applicable to service tax. These provisions have been listed out in the chapter on miscellaneous topics and readers may note that these provisions apply to service tax by virtue of Section 83 of Chapter V of Finance Act 1994 as amended from time to time. One of the sections of Central Excise Act 1944 which has been made applicable to service tax is Section 11B dealing with refunds under central excise. The same section would apply with regard to service tax as it would apply to duty of excise. Refund could be of service tax wrongly paid or paid in excess of the amount required to be paid or of cenvat credits accumulated on account of export of goods or taxable services. Refund of credits would be governed by Rule 5 of CCR 2004 under which Notification 5/2006 CE (NT) dated 14.03.2006 has been issued. As far as rebate is concerned, the central government has been empowered to notify the rules u/s 94. Rule 5 of Export of Service Rules 2005 framed in this regard allows the Government to come out with notifications in this regard and consequently, we have two notifications 11/2005 ST and 12/2005 ST on the subject of rebates.

How does the refund work?

The refund could be of service tax paid in excess or even of cenvat credits which are eligible for refund in accordance with Rule 5 of Cenvat Credit Rules 2004. While the refund claim on cenvat credits accumulated as per Rule 5 of CCR 2004 would be as per the procedure set out in Notification 5/2006 CE (NT), the refund claim on service tax should be made as per the procedure notified under the said section 11B. As per this Section, a claim for refund would generally have to be filed before the ACCE/DCCE before one year from the relevant date. The relevant date would depend on the event which necessitates the claim for refund. The relevant date generally would be the date of payment of service tax. Where the tax was paid provisionally, the date of adjustment of tax after final assessment, would be the relevant date. Where the tax becomes refundable as a result of an order or decree or judgment or direction of appellate authority or any court, the date of such order, decree or judgment or direction would be relevant. In case of an exemption order being passed u/s 93, the date of issue of such

order would be relevant. Where the services are exported in accordance with the Export of Service Rules 2005, the date of export of service would be the relevant date.

Procedure under sec 11B – Refund of service tax paid in excess

In terms of sec 83 of the Finance Act, sec 11B of the Central Excise Act would be applicable for refund of Service Tax. The refund under sec 11B read with sec 83 would apply even in cases where adjustment is not possible rule 6(3) or rule 6(4A) of Service Tax Rules.

Procedure for filing refund claim

- The person claiming refund may make an application for refund to ACCE or DCCE.
- The assessee shall make an application within one year from the relevant date.
- Where the person makes an application for refund of any amount which is paid under protest, the limitation period of one year shall not apply.
- The limitation period of one year is to be calculated from the date of payment of service tax.
- The application shall be made in Form R in triplicate
- The refund application shall be accompanied by such documents to establish that the amount in relation to refund are collected from or paid by him and the incidence of tax has not been passed on to the customer and there is no unjust enrichment.
- The applicant shall clearly state the facts and grounds to substantiate the refund claim.

Procedure for refund of credits u/r 5 of CCR 2004

- The claims are to be made once in a quarter in the calendar year (unless the assessee is an 100% EOU or exports in preceding quarter exceeded 50% of total value, when it can be made monthly)
- The service provider shall submit an application in Form A to the jurisdictional ACCE/DCCE within the time specified u/s 11B of CEA 1944
- The claim shall be accompanied by a copy of the invoice and a bank certificate certifying realization of export proceeds.

- The refund of unutilized input service credits would be as per the formula – (Total Cenvat Credit on input services during the period X (Export Turnover/Total Turnover))
- The service provider shall ensure proper follow up with the authorities till granting of refund.

Note: - The assesseees are also advised to submit copies of cenvat registers plus documents on which credits are taken as these may practically be required. The proof as to payment of amounts to the service provider on these bills on which credits are taken, would also have to be furnished to facilitate quicker refunds. Readers may also note that there is a view which regards the time limit of one year as per Section 11B of CEA 1944 as not being applicable to refund of accumulated cenvat credits as credits are to be distinguished from duty paid. The decision of the Gujarat High Court in *Swagat Synthetics Vs CCE Surat* (2008 (232) ELT 413 (Guj)) can be relied on in this regard.

Issues

Whether the time limit of one year is applicable to refunds of service tax paid in excess?

Readers may note that this has already been dealt with by the Tribunal/Courts. The Delhi Tribunal in *Indian Ispat Works (P) Ltd Vs CCE Raipur* (2006 (03) STR 161 (Tri-Del)) had held that where service tax was not payable, the department had no authority under law to collect the same and therefore the time limit of one year for refund was not applicable. Thus this question is a valid one and the view can be taken by assesseees.

Whether refund of accumulated credits possible?

In *Idol textiles Ltd Vs CCE Thane* (2007 (217) ELT 299 (Tri-Mum)), Rule 5 of Cenvat Credit Rules was held to be a beneficiary piece of legislation and refund of accumulated credit held to be available despite home consumption as it was a substantive right of the assessee. Therefore assesseees having accumulated credits on account of exports (goods or taxable services) could go in for the refund option

The claim should normally be accompanied by full documentary proof regarding the payment of appropriate taxes on which the claim for refund is being filed. The refund can be denied where any of the required conditions are not satisfied. The refund would be granted once an order for the same is passed by the concerned authority. Where the

order is against the assessee the same would have to be taken up on appeal with the Commissioner (Appeals).

Where the refund is not granted within three months from the date of application for the same or from the date of the order passed by Commissioner Appeals/Appellate Tribunal/Court, interest shall be payable as per section 11BB of Central Excise Act 1944 from the first day after the expiry of three month period and up to the date of refund at the rates notified which is currently at 6% p.a under Notification 67/2003 CE (NT) dated 12.09.2003

- The service tax provisions provide an option for the provider of taxable service who exports his services in accordance with the Export of Service Rules 2005 to opt for refund of the cenvat credits in respect of excise duty paid on inputs and service tax paid on input services (under Rule 5 of CCR 2004) used for providing such taxable services which are exported. This would be useful where the service provider is not in a position to utilise the said credits towards his liability on services provided within the country. Apart from this there is also an option to go for rebates (the procedure for which is explained in this chapter).

Refund of the service tax paid on specified services received for export of goods

Refund of the service tax paid on certain specified services used by exporters of goods for the purpose of exporting their goods would be available under notification 17/2009 ST dated 07.07.09. This notification has replaced the earlier Notification 41/2007 ST which dealt with the same subject. The features are explained below -

Conditions to be noted

- Cenvat credit of service tax actually paid on the specified services received should not be taken if refund is to be claimed
- The notification provides for a scheme of refund of service tax paid and not exemption from service tax altogether
- The services received are to be ones specified under the notification and used for export of goods
- Refund claim should not be for an amount less than Rupees five hundred
- Where the refund claim does not exceed 0.25% of the total declared FOB value of exports and where the exporter is registered under EPC sponsored by Ministry of

Commerce or Ministry of textiles, the claim shall be accompanied by necessary documents and a certificate to the effect that the specified service has been received and service tax paid thereon and the said service used for export of goods. The certificate shall be by the proprietor or the person authorized by the Board of Directors as applicable.

- Where the claim exceeds 0.25% of total declared FOB value of exports, the certification would be by the Chartered Accountant auditing the books of the company under Income Tax Act 1961 or Companies Act 1956.

Procedure to be followed

- Where the exporter is not a manufacturer registered under CE, he shall before filing the claim, file a declaration in form A 2 with the ACCE/DCCE having jurisdiction over his Registered office or Head Office
- The exporter not having excise registration who has filed form A 2 would receive a Service Tax Code within 7 days from the said ACCE/DCCE
- The next step would be to file the refund claim in Form A 1 with the said authority (ACCE/DCCE). A manufacturer exporter who would have Central Excise registration would directly file Form A 1 with the ACCE/DCCE having jurisdiction over his factory and would not be required to file form A 2.
- The claim for refund would have to be made within one year from the date of export of said goods i.e date of clearance u/s 51 for export of goods by the proper officer of Customs
- The claim shall be accompanied by all the necessary documents proving receipt of specified service, payment of service tax, usage of service for export of goods with Shipping Bill reference including the documentation as required in the table below plus certification as explained earlier
- The refund would be within one month of claim if ACCE/DCCE is satisfied with the same. Where not sanctioned, the reasons are to be in writing
- The exporter shall ensure that the proceeds for export are realized within the time limit specified under FEMA 1999 failing which the service tax refund would be recoverable.

Readers may refer the stated notification on www.cbce.gov.in for getting the list of documents required to be filed with the refund claim to avoid a scenario where the claims are stuck for want of details.

Procedure for Claiming the Refund under notification 9/2009 ST dated 03.03.09 by SEZ unit/developer

- The developer or unit in SEZ shall claim the exemption by filing a claim for refund of service tax paid on specified taxable service.
- The developer or units in SEZ shall file the claim for refund to the jurisdictional Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise as the case may be.
- The developer or the units in SEZ who is neither registered as an assessee under the Central Excise nor Under Service Tax Law, has to file a declaration in form annexed to the notification (Form available on www.cbec.gov.in) to the jurisdictional Assistant Commissioner or Deputy Commissioner of Central Excise.
- The jurisdictional Assistant Commissioner or Deputy Commissioner shall after due verification allot a service tax code (STC) number to the developer or units of SEZ within seven days from the date of receipt of said form.
- The claim for refund has to be filed within six months or such extended period as the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise as the case may be permit from the date of actual payment of service tax by such developer or unit to service provider.
- The Claim for refund shall be accompanied by the following documents:
 - i. A copy of the list of specified services required in relation to the authorized operations in the Special Economic Zone as approved by the Approval Committee.
 - ii. Payment of Service Tax on the specified services for which claim for refund of service tax paid is filed (Invoice of the service provider and the proof of payment for the said invoice).
 - iii. A declaration to the effect that such services received by the developer or unit in SEZ are used in relation to the authorized operation in SEZ.
- The Assistant Commissioner or the Deputy Commissioner after **satisfying** that the said services have been actually used in relation to authorized operations in SEZ, refund the service tax paid on the specified services.

Refund under notification 43/2007-ST-Available to manufacturers of specified goods in respect of business exhibition service

Conditions

- This notification exempts the services provided by the organizer in relation to business exhibition services of goods
- Prior to availment of the benefit under this notification, the manufacturer should have exported the goods falling under chapter 57, 61, 62 and 63 of Central Excise Tariff Act.
- The manufacturer has to register himself with any of the following organizations
 - (i) Apparel Export Promotion Council;
 - (ii) Carpet Export Promotion Council;
 - (iii) The Cotton Textiles Export Promotion Council;
 - (iv) Handloom Export Promotion Council;
 - (v) The Indian Silk Export Promotion Council;
 - (vi) Powerloom Development & Export Promotion Council;
 - (vii) Synthetic & Rayon Textiles Export Promotion Council;
 - (viii) Wool & Woollens Export Promotion Council;
 - (ix) Wool Industry Export Promotion Council;
 - (x) Jute Manufacturers Development Council;
- The exemption shall be by the way of refund of service tax paid on Business Exhibition service
- The manufacturer claiming the refund should have made the payment to the service provider.
- Once the benefit under this notification is claimed, no Cenvat credit under rule 3 should be claimed under Cenvat Credit Rules 2004.

This exemption was till 31.03.09 and one would have to see whether the same would be extended.

Procedure for filing the refund claim

- The said manufacturer shall file the refund claim to the ACCE or DCCE, as the case may be, having jurisdiction over the factory of manufacture or warehouse.
- The refund claim should be accompanied by such documents evidencing the payment of service tax to such service provider.
- The ACCE or DCCE, as the case may be, shall, after satisfying himself that the said service has been actually used by the said manufacturer in relation to business exhibition of the said goods manufactured by him, refund the service tax paid on the said service.
- The benefit under notification is available upto 31st March 2009.

How does the scheme of rebate work?

The rebate can be granted by the central government either on the service tax paid on taxable service exported or service tax paid on input services and/or duty paid on inputs used in providing such taxable service. This rebate shall be subject to conditions and limitations specified in the concerned notification dealing with the rebate.

Rebate of the service tax on taxable services exported

Notification 11/2005 ST dated 19.04.05 as amended grants rebate of service tax and cess (including SHE cess) paid on all taxable services (output services) exported in terms of rule 3 of Export of Services Rules 2005, to any country other than Nepal and Bhutan subject to conditions specified below –

- The taxable service has been exported in terms of rule 3 of the aforesaid rules
- The payment for export of such taxable service has been received in India in convertible foreign exchange
- The service tax and cess of which rebate has been claimed has been paid on the taxable service exported
- The rebate of service tax and cess is not less than rupees five hundred

Where the service tax and cess (including SHE cess) of which rebate has been claimed has not been paid or the taxable service has not been exported, the rebate allowed shall be recoverable with interest.

Procedure for the same -

- The claim for rebate shall be filed with the jurisdictional Assistant Commissioner or Deputy Commissioner of Central Excise in Form ASTR 1
- The application shall be accompanied by a documentary evidence of receipt of payment against the taxable service exported and the payment of service tax and cess on such taxable service exported.
- There shall also be a declaration that the taxable service has been exported in terms of rule 3 of Export of Services Rules 2005 along with the documents evidencing the export of such taxable service.
- The jurisdictional ACCE/DCCE if satisfied that the claim is in order, shall sanction the rebate either in whole or in part.

Note: - The assesseees are also advised to submit the details as to cenvat credits availed with the payments made to the service provider, to facilitate quicker rebate. For this, a cenvat register giving details of the credits availed plus details of the debits against the credits on export of taxable service would have to be maintained. This should be backed up with other documentary evidence in the form of invoices for export, bills for claiming credit, proof of payment to service provider, export realization, etc.

Rebate of the service tax on input services or duty on inputs

Notification 12/2005 ST dated 19.04.05 grants rebate of the whole of duty paid on excisable inputs or whole of service tax and cess (including SHE cess) paid on all taxable input services used in providing taxable service exported in terms of rule 3 of Export of Services Rules 2005, to any country other than Nepal and Bhutan subject to conditions specified below –

- The taxable service has been exported in terms of rule 3 of Export of Service Rule 2005
- The payment for export has been received in India in convertible foreign exchange
- The duty, the rebate of which has been claimed, has been paid on the inputs
- The service tax and cess, the rebate of which has been claimed, have been paid on the input services
- The total amount of rebate of duty, service tax and cess admissible is not less than rupees five hundred
- Cenvat credit should not have been availed on inputs and input services on which rebate is claimed

Where the duty or the service tax, rebate of which has been claimed, have not been paid or the taxable service has not been exported or the cenvat credit has been availed on inputs and input services on which rebate has been claimed, the rebate shall be recoverable with interest.

Procedure for the same -

- The provider of taxable shall, *before the date of export of taxable service*, file a declaration with the jurisdictional ACCE/DCCE describing the taxable services to be exported.
- The declaration shall be accompanied by -
 1. A description, quantity, value, rate of duty and the amount of duty payable on the inputs actually required to be used in providing taxable service to be exported.
 2. In case of input services, the description, value and the amount of service tax and cess payable on input services actually required to be used in providing taxable services to be exported shall also be given.
- The ACCE/DCCE shall verify the correctness of the declaration and may accept the declaration on being satisfied as to the truth of its contents.
- The inputs shall be procured directly from a registered factory or from a registered dealer accompanied by valid invoices issued under Central Excise Rules 2002
- The input services shall be received along with an invoice, bill or a challan as per the provisions of Service Tax Rules 1994
- The claim for rebate of duty paid on inputs or service tax and cess paid on input services shall be filed with jurisdictional ACCE/DCCE in Form ASTR 2
- The application has to be accompanied by invoices issued under Central Excise Rules 2002 for procurement of inputs, invoices for input services as per Service Tax Rules 1994 , plus documentary proof for payment of duty on inputs and service tax on input services
- Proof of receipt of payment against service exported in convertible foreign exchange
- A declaration shall also be filed stating the service has actually been exported in terms of rule 3 of the Export of Service Rules 2005
- Proof of such export of service

Where the claim is in order, the jurisdictional ACCE/DCCE shall sanction the rebate either in whole or in part.

CHAPTER 9. DEMANDS AND APPEALS

Service providers who also happen to be manufacturers registered under the Central Excise Act 1944, may be familiar with the recovery proceedings under Central Excise. Such assessees would not find the proceedings under service tax intimidating as the procedures are similar. However, it has been observed that assesses who are new to service tax, dread recovery proceedings and the thought of having to face a Show Cause Notice from the department. This fear is at times misused by few unscrupulous officers.

What happens when there is a short levy or short payment of tax or erroneous refund?

Section 73 of Chapter V of Finance Act 1994 as amended from time to time deals with such a scenario where there is case of short payment of service tax or short levy or erroneous refund of tax. In such cases, the Central Excise Officer may within one year from the relevant date, serve a notice on the assessee/person chargeable with such service tax requiring him to show cause as to why he should not pay the amount specified in the notice. The period of one year for issuing such SCN (Show Cause Notice) can be extended up to five years in a case where such non-levy/short levy/erroneous refund/short payment was on account of fraud, collusion, wilful mis-statement or suppression of facts or contravention of any of the provisions of this Chapter or of the Rules made thereunder with the intention to evade payment of service tax. While computing the period of one year/five years the period for which the service of notice is stayed by an order of a court, shall be excluded.

The assessee would then have to furnish his replies to the said SCN within the time set out in the notice.

Where there is a non-levy, short levy or erroneous refund, the assessee himself can pay the amounts due after ascertaining the dues himself and intimate the Central Excise Officer in writing who shall then not serve a SCN in respect of such amount paid. The Officer is empowered to determine the correct amount and issue SCN for the recovery of

the same and in such cases, the period of one year can be from the date of intimation of payment as stated earlier, by the assessee.

As per section 73(1A), where the non-levy, short levy, erroneous refund was on account of fraud, collusion etc., the assessee can pay the service tax amount in full as per the SCN issued along with the interest u/s 75 and penalty at 25% of the amount of service tax, within 30 days of the receipt of such notice and where so paid, the proceedings initiated shall conclude. Where service tax is paid in part, the Central Excise Officer can continue the proceedings to recover the balance amount due as per the SCN.

What happens when the service provider has collected service tax in excess of the amounts to be collected from the service receiver?

Section 73A deals with such a scenario and the service provider would have to pay the amounts so collected to the Central Government. Where not paid, a SCN can be issued with regard to recovery of such amounts. This provision would apply in all such cases where the service provider has collected in any manner from the service receiver, amounts representing service tax. Once the assessments have been finalised and if the amounts paid have been found to have been paid in excess, a refund claim can be filed for the same within six months from the date of notice by Central Excise Officer.

What is the interest for delay in payment or in cases where amounts have been collected in excess from customers?

The interest rate would have to be adopted in accordance with rate notified u/s 75 and 73B. The rate for both cases at present is 13% per annum.

Is provisional attachment of property possible?

Section 73C makes provisional attachment of property possible during pendency of proceedings u/s 73 or 73A. This can be done to protect the interests of revenue but with the permission of Commissioner of Central Excise. The attachment shall be by an order in writing and of property belonging to the person on whom the SCN is served. The attachment shall be only for six months from the date of the order unless extended by the Chief Commissioner of Central Excise.

Can mistakes apparent from record be rectified?

An order can be amended by the Central Excise Officer within two years from the date of passing the same to correct a mistake apparent from the record, u/s 74. Where any matter has been considered and decided by way of Appeal or Revision relating to the order referred above, any other matter on the order can be rectified with the exception of the matter that has been so decided. Amendment can be on one's own motion or through notice by assessee or CCE/CCE (Appeals). Where the rectification has the effect of reducing refund due to an assessee or increasing his liability, such assessee should be given a reasonable opportunity of being heard in the matter.

Determination of Points by the CCE (Appeals)

Under Section 84, the CCE may on his own motion, call for the record of any proceeding in which an adjudicating authority subordinate to him has passed an order or decision under the provisions of this Chapter. For the purpose of satisfying himself as to legality or propriety of such order, he can direct such authority or Central excise Officer subordinate to him, to apply to CCE (Appeals) for determination of such points arising from the decision or order as indicated by him.

Where the assessee is aggrieved by the order of an authority subordinate to Commissioner of Central Excise, where would the appeal be made?

As per section 85, the appeals shall be with CCE (Appeals). The Appeal shall be within three months from the date of receipt of the decision or order of such authority. Where the assessee has reasonable cause for delay in filing the appeal, the time limit can be extended by CCE (Appeals) for further period of 3 months. Beyond the said 3 months there is no provision for condonation of delay. Supreme Court has ruled that beyond that period no condonation is possible. Orders would be passed in writing after a proper hearing.

When shall the appeal be with the Appellate Tribunal?

The appeal shall be against the order passed by the Commissioner of Central Excise or the CCE (Appeals). The appeal shall be within three months from the date of the order sought to be appealed against. The respondent shall then be required to file a memorandum of cross objections within 45 days of the receipt of notice as to appeal by

the appellant. The prescribed fee would have to be paid at the time of Appeal. The scale would be as follows -

- Where the amount of tax + interest + penalty is Rs. 5 lakhs or less – Rs. 1000/-
- Where the amount of tax+ interest + penalty is more than Rs. 5 lakhs but less than Rs. 50 lakhs – Rs. 5000/-
- Where the amount of tax + interest + penalty is more than Rs. 50 lakhs – Rs. 10000/-

The application for grant of stay, rectification of mistakes, restoration of appeal or an application or any other purpose would have a fee of Rs. 500/-

The Board is also empowered to constitute a Committee of Commissioners/Chief Commissioners to refer matters to Board or to jurisdictional Chief Commissioner where it differs with the order passed by CCE or CCE (Appeals)

Where appeals are filed, the amount of tax in dispute would have to be deposited by the assessee unless it can cause undue hardship in which case, an application would have to be filed with the CCE (Appeals) or the Appellate Tribunal as the case may be for dispensing with the requirement by virtue of section 35F of CEA 1944 read with section 83.

Appeal to High Court

The appeal can be made against the order of the Appellate Tribunal when it involves a substantial question of law. Whether it involves a substantial question of law or not is something to be decided by the High Court. The appeal is to be made within 180 days from the date of receipt of the order sought to be appealed against with a fee of rupees 200 u/s 35G of CEA 1944 read with section 83 of Chapter V of Finance Act 1994 as amended from time to time. The High Court may even determine an issue which has not been determined by the Appellate Tribunal. The order of the High Court shall be appealable to the Supreme Court if the High Court certifies it to be fit for appeal.

CHAPTER 10. PROCEDURES WITH REGARD TO REGISTRATION

The provisions under service tax with regard to registration not only require the assessee to register himself when he starts providing a taxable service, but also to amend his certificate of registration every time there is a change in his business profile. He is also required to state at the time of registering as whether he wants to opt for centralized registration or not. This option can be exercised even at a later date in which case, he would have to get his Registration Certificate amended. Apart from a service provider, even a service receiver who is liable to pay service tax u/s 68(2) of Chapter V of Finance Act 1994 would be required to register himself under service tax for the purpose of paying service tax. The requirement as to registration would also extend to an Input Service Distributor who would want to distribute Cenvat credits on inputs, input services or capital goods to the unit providing taxable service or engaging in manufacturing of dutiable final products. The procedures with regard to registration under service tax in each of the scenarios would basically be the same with very minor changes which would be evident on the application for registration.

What is the procedure for registration?

1. The assessee shall make an application in form ST 1 to the Superintendent of Central Excise in duplicate.
2. The application shall be filed within 30 days from the date of providing taxable service and shall bear the address sought to be registered
3. The application should be filled up carefully without errors and columns and boxes which are not applicable may contain "NA" stated across them. All the taxable services provided should be mentioned on the application and there would not be separate applications for each of such taxable services
4. The Form should be signed by the director/partner/sole proprietor as the case may be or the authorized signatory.
5. The application shall be accompanied by copies of the following documents -
 - Self certified copy of PAN, (where allotment is pending, copy of the application for PAN may be given)

- Copy of MOA/AOA in case of Companies
 - Copy of Board Resolution in case of Companies
 - Copy of Lease deed/Rental agreement of the premises
 - A brief technical write up on the services provided
 - Registration certificate of Partnership firm
 - Copy of a valid Power of Attorney where the owner/MD/Managing Partner does not file the application
6. Once filed, the acknowledgement for having filed the application is to be obtained on the duplicate copy for one's own reference
7. If the Particulars stated in the Form are correct, then the registration certificate would be provided within a period of seven days. Where not so provided, the registration is deemed to have been granted.

How is centralized registration different?

Centralised registration is opted for in a case where the accounting and billing operations of the assessee are centralized in an administrative office which may be a branch or Head Office despite the services being provided from more than one location. The premises that is registered here is the one where the centralized accounting and billing is done. This decision is at the option of the tax payer and he can also opt to have multiple registration which however may not be advisable.

The procedure would be the same as explained above with a few exceptions -

- The registration in case of centralized registration would be granted by the Commissioner of Central Excise having jurisdiction over the centralized premises
- The registration formality at the department's end takes a little longer than the period stated above and the concept of deemed registration need not apply here

The following documents are required in addition to the documents needed under the aforesaid procedure -

- a. Proof of address of each such premises or branches for which centralised registration is sought
- b. Proof of address of branches, new offices opened if any

How to make amendments with regard to changes in particulars?

Amendment would be required where there is any change in the particulars furnished in the ST 1 at the time of registration.

- The changes shall be intimated to the department within 30 days of such change
- The fact that the ST 1 is being filed for an amendment, should be clearly highlighted on the form
- The assessee shall submit a certified copy of the Registration Certificate
- The application may also be accompanied by a covering note explaining the circumstances that led to the change with copies of relevant documents being given.

CHAPTER 11. PROCEDURE WITH REGARD TO INVOICING

The invoicing procedure with regard to service tax is something that is not assigned adequate importance by certain service providers. As far as possible where the records of the assessee are fully computerized, invoices may be generated from the system itself. Many of the accounting packages available in the country support invoicing and the invoicing option using the software may be selected. But in quite a few cases it has been found that though the records of the assessee are computerized, the invoicing is manual or through independent software package leading to unconnected islands, which do not speak to each other. At times the choice of invoicing method / formats may be at the behest of the customers.

How to raise a proper invoice?

The assessee can follow the guidelines laid down below for the purpose of ensuring a proper invoicing methodology. The invoicing requirement is governed by Rule 4A of Service Tax Rules 1994.

- The invoice is to be issued within 14 days of completion of taxable service or receipt of amount whichever is earlier.
- The invoice / bill / challan should be signed by such service provider or a person authorised by him.
- The invoice shall be serially numbered and should contain the following information -
 - The name, address and registration number of the service provider.
 - The name and address of the service receiver
 - Date of raising of invoice
 - Details of the customer's/client's work order/purchase order
 - Description, classification and value of taxable service provided.
 - The amount of ST and Education cess/SHE Cess charged on such service tax
- Break up of the amount charged towards the service
- Details as to exemption being claimed with reference to the concerned notification

Note: - The assessee is advised to indicate the values clearly where he claims deduction for value of goods or materials transferred during the course of providing the service. If he is following the benefit of notification 12/2003 ST, the material value is to be indicated

clearly so as to avoid disputes with the department. The service provider is also required to raise an invoice on receipt of advances towards the taxable services to be provided though very few assesseees practically follow this requirement.

CHAPTER 12. RECORD KEEPING

Record keeping under service tax is one of the most critical factors from the point of view of compliance. The assessee should have a sound record-keeping system if he is to avoid a scenario where he struggles at a later date to ensure compliance with the law. Considering the level and scale of computerization in India, it is shocking to note that the assessee who struggle the most with record keeping are those who have fully computerized system or even the ERP environment. Quite often assessee end up using customized software either developed in-house or sourced from abroad, which do not fully cater to the reporting requirements under service tax. Surprisingly the entire indirect tax compliance would be outside the ERP, which means that none of the checks and balances is within the system.

Assessee also struggle due to ignorance as to the provisions of law as well as to the reporting requirements thereunder. Until and unless the assessee himself is clear about the concepts of service tax and the reporting requirements thereunder, he would not be in a position to educate the systems analysts and the programmers to make changes to the software in order to ensure better reporting.

What are the records to be kept and whether there are any statutory records to be maintained?

There is no statutory record prescribed under service tax as far as record keeping is concerned. The assessee should follow the basic guidelines laid down here –

- A proper record should be kept of the materials received and used for the purpose of providing taxable services. The basic documents for this would be the Goods Received Notes and the Raw materials ledger in stores. Where the service provider has both taxable as well as exempted services, separate material accounts may be kept and Cenvat credits availed only on those materials used for providing taxable services. This can be done by segregating the material receipts at the GRN stage itself by having separate series for materials meant for use in taxable services. This should be followed up with proper physical control over stocks. Where stocks are transferred from one location to another, a system of having requisition slips can be followed in

addition to stock transfer notes/invoices which would indicate the intended usage of the stocks so transferred.

- Next would be the task of identifying the input services to be used for providing services. To the extent possible, the services to be used for providing taxable services should be identified so that full credits can be claimed on the same. Where segregation is not possible, the same would have to be flagged off for applying the formula laid down in Rule 6 of CCR 2004
- As far as input services are concerned, they may be assigned codes while accounting the same in the financial ledgers to identify them in terms of the intended usage. Another effective way of doing this is by documenting the reasons for procuring the service at the time of raising of the work order on vendors/service providers which would facilitate proper tracking of such input services at subsequent stages.
- Proper recording of Cenvat credits in respect of inputs and input services. The assessee here can maintain a Cenvat credit register which would give in detail the amounts of credits availed. The register can furnish the following details – Entry serial number, vendor name, item description and description of input service, basic value of goods/services, basic excise duty or service tax, cess on duty/tax, GRN reference for receipts, payment reference for having paid the service charges + service tax to the input service provider, total credits available, amount debited, invoice/bill for such debit, closing balance of credits. The assessee should also record the credit figures correctly in financial ledgers which can then facilitate a system of reconciliation between the Cenvat registers and the financial ledgers.
- Care should be taken with regard to invoicing to ensure that proper breakups are given for the values so that the correct amount liable to service tax may be determined. For the purpose of filing of the ST 3 returns, detailed work sheets would have to be maintained clearly indicating the value of services billed, the amounts received towards such services billed, the amount of VAT/sales tax paid, the value of materials sold and the amounts charged towards labour so that the correct amount of service tax payable may be ascertained.
- The assessee should also have a proper referencing system through which the various documents are linked. This linking can be brought about through quoting

the bill numbers and the voucher references on the registers being maintained which would also ensure that no bill or voucher has been left out.

- The list of records is to be declared within the end of the month in which the first return is being filed.

CHAPTER 13. PAYMENT OF SERVICE TAX

Service tax is payable on the amount or value of taxable service received and not on the gross amount billed. But even today there are quite a few assessees who pay on the amount billed. In case any advance is received for service to be provided then the service provider shall pay the service tax on the amount received. Where the service is not provided and the amounts are refunded to the payer, such service tax paid can be adjusted in the returns by the assessee.

Service tax is to be paid on the gross value of taxable service, and not on the net amount realized from the service receiver after TDS under Income Tax Act 1961.

The service tax amount collected during the calendar month has to be paid to the credit of central government by 5th of the subsequent month (6th of the subsequent month if done electronically) and the amount is to be paid by 31st of March for the month of March of the financial year.

If the service provider happens to be individual or proprietary firm or partnership firm the service tax amount has to be paid by 5th of the subsequent month, following the quarter (6th of the month following the quarter if done electronically) and 31st of March for the quarter ending March of the financial year. When the payment is made through cheque, then the date of presentation shall be deemed to be the date of payment.

How to pay service tax?

- The service provider shall himself assess the tax payable for the month or quarter as the case may be on the basis of the amounts received towards taxable services
- He shall then ascertain the amount of credits left in balance at the end of the period stated above for which payment is being made. He shall then reduce the credits balance to the extent available or to the extent of his liability whichever is lesser
- Where any amount is remaining payable after the adjustment discussed above against the credits, the same shall be remitted within the due dates explained above.

- The amount shall be paid into the designated bank account using the form GAR 7 which is filled up. The amounts are to be rounded off to the nearest rupee. Separate accounting codes have been notified for service tax, education cess, secondary and higher education cess, interest, penalties etc. The service provider remitting the tax shall segregate these amounts and pay the same under the respective codes

Note: - If excess payment is made, then the amount paid in excess shall be adjusted in the subsequent month provided the excess payment is not more than one lakh due to arithmetical error.

For the service providers paying service tax amount exceeding fifty lakhs and above during the preceding previous year, the service tax liability shall be remitted through e-payment. Penalty of Rs. 5000/- is leviable for failure to make payment through e-payment u/s 77(1)(d)

The service provider on his failure to pay the amount within the notified date shall be liable to pay interest at the rate of 13% p.a.

If the service provider is unable to quantify the amount of service tax payable, then he may request AC/DC of Central Excise to allow the service provider to pay on provisional basis along with the reasons.

Now rule 6(1A) allows the service providers liable to pay service tax to make the payment in advance and adjust the same for the liability in subsequent period. However such payment in advance has to be intimated to the department within 15 days from the date of making such payment and the details of such advance payment and adjustment thereof shall be indicated in the returns.

CHAPTER 14. SERVICE TAX RETURNS

Filing of service tax returns has been one aspect in service tax compliance which has been posing considerable problems for assesseees. One of the main reasons is that service tax has to be paid not on billing basis but on receipt of consideration from customers. Thus all organizations especially those where transaction are in thousands should have a good accounting system in order to enable them to link the bills with the amounts received. The concept sounds simple but few organisations really implement the same in spirit. As a result, they face considerable problems in filing the service tax returns as one is expected to give details as to the amounts received towards taxable services.

The delays in filing entail fines and non filing an enquiry under best judgment.. Other than that it would be one of the criterion for picking up the unit for audit under the risk based selection proposed for the service tax audit.

How to file the service tax return?

- Form ST 3 or ST 3A as the case may be has to be filed in triplicate to the Superintendent of Central Excise
- The return has to be filed once in six months and it contains the particulars of all the six months
- The value of taxable services should be computed on the basis of gross amount received or advance received for the services provided/to be provided
- A nil return is required to be filed if there are no transactions
- GAR 7 evidencing payment has to be filed along with the return
- If any amount representing interest or penalty is paid, then references of such payment along with the particulars are required to be made.
- The ST 3 return is to be submitted within 25th of the subsequent month following the quarter i.e. For the half year April to September, the due date is 25th of October and 25th of April for the next half year.
- If the day happens to be a public holiday, then the return can be submitted on the next working day immediately following the holiday.
- The return may either be submitted in hand or sent through Registered Post Acknowledgement Due

Can a revised return be filed?

Yes. Rule 7B of Service tax Rules 1994 allow an assessee to revise the return filed under Rule 7 to correct any error, omission or mistake within 90 days from the date of filing the return u/r 7.

Where the time limit has expired the authors are of the view that the same the revised retron can still be filed as a measure fo disclosure which would normally be accepted.

Note: -

- *An annexure is provided to the said form (ST 3 return) providing tips for filing up the particulars of the return*
- *The form can be downloaded from the departmental website (www.cbec.gov.in)*
- *ST 3A is used when the assessee opts for provisional assessment. The assessee shall for this purpose make a request in writing to the ACCE/DCCE giving reasons for payment of service tax on provisional basis and the payment can be made on the taxable value as specified by ACCE/DCCE on provisional basis. The assessment would be finalised later and the provisions of Central Excise Rules with regard to provisional assessment would apply here. However, execution of bond would not be required here.*
- *A single return is sufficient even though the service provider is providing more than one taxable service.*
- *The ST 3 return can either be filed manually or electronically*

CHAPTER 15. SERVICE TAX AUDITS BY PROFESSIONALS

A service provider simply cannot ignore compliance with the legal provisions for the simple reason that if he does so, the non-compliance could hit his business hard considering the competitive margins involved as well as the impact of interest and penalty which are becoming increasingly harsh day by day.

It has been the experience that very often assessees are not even aware of the fact that they are not complying with the legal provisions till such time when they are called upon by the department to furnish some clarifications or their unit is taken up for an audit.

Assessees in this regard should note that considering the uncertain nature of the law, the frequent amendments by way of notification, clarifications by the Tax Research Unit (TRU), Central Board of Excise & Customs (CBEC), Director General Service Tax (DGST) other than Regional Advisory Committee and Commissioners clarification the law would continue to be unclear. Many advocates of the Supreme Court with decades of standing in the Indirect taxes opine that there is no surety in this segment. Therefore a mechanism would have to be built in to ensure that compliance is maintained at high levels all the times. This would require a comprehensive framework to be put in place which would ensure proper training of employees as well as seeking professional opinion from time to time on matters of doubt plus a review of the documentation, records pertaining to service tax by either the internal audit team of the concern or by an independent professional.

What is required of the auditor?

An auditor who handles service tax should be thorough in his knowledge of the subject as well as the latest auditing procedures and techniques to be adopted so that he can maximize the benefits to his client from the audit exercise. Use of the audit tools especially the generalized audit software for large concerns would enhance the results. Apart from this he should have the ability to understand the assessee's business and the activities performed in order to study the impact of service tax on the same. As far as carrying out the audit itself is concerned, he can follow the guidelines given below:

1. Ascertaining scope of the assignment

The auditor should first of all be very clear as to the scope of the audit assignment. This is to avoid a scenario where the client perceives the audit effort in a different way from the one it actually is. This is quite common in the service sector as the concept of service tax audit is new to them as well as the fact that clients are specialists in their respective fields with no much of exposure to subject of accounting or auditing. At times the client may wish a pre- audit or shifting of the responsibility of compliance on the auditor. Further many a time assesseees in the service sector mistake auditing for outsourcing and expect the auditor to engage in an outsourcing job rather than reporting to the management on compliance related issues. The scope can be ascertained and confirmed by preparing a letter/scope document entailing the areas which would be covered and the aspects which would not be taken up during the audit.

2. Knowledge of the business and the activities performed

This is one of the most important aspects to be taken care of by the auditor. He/she should first of all understand the assessee's business, the services he provides, the activities that are involved at various levels of the organisation in providing these services, the customer profile whether sub contracted or not etc. before he can start his review/verification. For this purpose, he may interview the key management personnel in the organisation besides going through major contracts and agreements, organisation chart, manuals and publications of the organisation. He should also make it a point to visit the premises from where the services are provided, to the extent possible and interview the technicians / engineers who actually perform the tasks (where ever applicable) to get a first hand information of the nature of the processes involved in case of services of a technical nature.

3. Obtaining relevant information for a preliminary review and risk analysis

The auditor should make it a point to understand the financial performance of the entity in the recent past as well as the during the audit period, apart from analyzing the same so that he can devise his procedures accordingly. He/she should also make it a point to perform a quick review of the concerned records like the service tax returns, cenvat bills, invoices and agreements with major clients'/customers so that the risk arising from non-compliance can be assessed. The following aspects assume significance –

- Review of the past audited financial statements for understanding the past financial performance in terms of incomes, expenses, receipts and payments apart from accounting policies and nature of investments
- Review of the ledgers for the period under audit to check the income and expenditure pattern besides understanding the customer profile and the pattern of billing
- Review of the cenvat invoices, agreements with major customers, service bills raised on customers by the assessee, Excise invoices if any raised by the assessee, review of the fixed asset registers to form an idea as to record keeping and compliance with the law.

The auditor would have to document his findings so that he can effectively move on to the next stage.

4. Desk review of the information obtained and preliminary meeting

The auditor, on the basis of his/her findings at the previous stage, should carry out a desk review of the information available with him to arrive at proper conclusions as far as the possible risk levels involved, are concerned. The desk review should ideally indicate to the auditor the level of checking required and the areas he should concentrate upon in order to arrive at proper conclusions at the end of the audit. On the basis of the review he should document the risk level prevalent in the audit. Once this has been done, he should identify the audit team that would take up the task and discuss the preliminary findings with the members of the team to appraise them of the likely issues that could crop up during the audit apart from explaining the impact the legal provisions would have on the assessee's business and his activities.

5. Devising the audit programme for carrying out compliance and substantive tests

The auditor should devise a proper audit program only after carrying out a desk review so that the same would be more effective than a program which is common to all audits irrespective of the differences in services and related activities and the risk levels involved. This would enable the auditor to concentrate on key areas which would be relevant to arrive at proper conclusions at the end of the audit. The audit programme should indicate the areas to be covered and the individuals who are supposed to take it up.

6. Documentation and proper supervision of audit effort

The auditor should ensure that the audit findings and the explanations given from the assessee's side are documented properly by his audit team. The team should ideally consist of individuals at various stages of a learning curve. The team can consist of three members with one of the members being a senior with sufficient experience and two juniors. The responsibility of supervising the team on a daily basis would be with the senior and the entire audit effort would have to be supervised at regular intervals by the qualified professional. The audit findings should be discussed at periodic intervals (if not on daily basis) with the executive designated from the assessee's side so as to ensure assessee's cooperation. This would also ensure that the audit is headed along the right path with every likely-hood of achieving its intended objectives at the conclusion stage.

7. Formulation of the draft report and discussions with the management

Once the audit has been completed, the draft report containing the draft of the observations should be formulated and a copy sent to the management. This would then be followed up with a discussion of the points in order to ascertain the future course of action to be taken, which should also be documented. The auditor could come up with valuable suggestions here in order to secure effective compliance with the law and in order to avoid pit falls in future. This discussion is critical for the acceptance of the observation and its correction.

8. Finalising the draft and ensuring audit follow up

Once the draft has been prepared, the points discussed with the management and future course of action ascertained, the final report is to be sent with all the relevant details like the observations, the reply from the assessee's side, the corrective action taken up by the assessee, the course of action which is to be taken in the future. The auditor's responsibility does not end here and he would have to ensure proper follow up by going through the steps taken up by the assessee for the purpose of ensuring compliance with the law.

Pointers for practice

- The auditor should be well versed in the matters pertaining to service tax and to a certain extent central excise and should have a clear understanding of the legal

provisions and its possible implications on an assessee's business depending upon the activities performed.

- He should have the ability to get the required information from the assessee in a way that would enable him to ascertain the legal impact on the assessee's business. This in fact could be a big challenge as he would have to pose his queries in a way the assessee understands the same so that the right answers and explanations can be obtained from him.
- The auditor should also be careful not to treat the audit like a fault finding exercise as it would result in the client losing interest in the audit itself and thereby negating the very purpose of audit.
- These audits could be said to be consultative exercise as differentiated from a regular internal audit. Therefore it maybe a good idea for the auditor to appraise the client on the latest amendments and Tribunal judgments in regard to the issues of interest/ concerns.

CHAPTER 16. FREQUENT ERRORS COMMITTED IN SERVICE TAX

Since service tax was introduced recently as compared to Central Excise Act and Customs Act which have been in force for more than three decades now, and since the subject has been seeing a lot of changes every year, the chances of the assesseees (especially those who are new to service tax) going wrong or committing mistakes at the initial stages of compliance are quite high. In this segment we shall take a close look at some of the errors we have noticed from the assesseees. The assesseees are advised to be careful in this regard to ensure that they do not commit the mistakes given here –

1. Wrongly classifying the services under a category which is not applicable to them.
2. Wrong availment of cenvat credit on ineligible documents.
3. Wrong availment of cenvat credits on services which do not qualify as input services within the definition of input service as given in Cenvat Credit Rules 2004
4. Short payment or excess payment of service tax due to improper accounting of the amounts collected from the customers/clients especially on account of service tax
5. Mistakes being committed while filling up the ST 3 returns with regard to the value of taxable services, amounts received and the exemptions availed
6. Treating the services provided from India to a person abroad as Export of Service when it is not an export of service as per Export of Service Rules 2005
7. Failing to pay tax u/s 68(2) on services received in India from abroad when the same constitutes an import of service
8. Paying service tax on the gross value including amounts charged for transfer of property in goods when the assessee could have claimed deduction for such transfer of property in goods
9. Exporting services but not going in for either the rebate of service tax under Export of Service Rules or refund under Cenvat Credit Rules
10. Claiming full cenvat credit when the service provider has both taxable as well as exempted services

11. Utilising the cenvat credits in respect of the exempted services which are exported
12. Paying service tax as well as excise duty on service charges where the manufactured goods are installed at the customer's premises
13. Excluding the expenses reimbursed by the service receiver from the purview of service tax where the same is not incurred by the service provider as a pure agent of the service receiver
14. Non segregation of the education cess and Secondary Higher Education cess amounts from the basic portion of service tax
15. Not fulfilling the conditions laid down by the exemption notifications while claiming exemption benefits
16. Collecting service tax from the customers/clients but not paying the same to the government
17. Not registering and paying service tax in respect of those services where the service receiver is liable to pay tax u/s 68(2)
18. Availing input service credits before the payments of service tax and value of services can be made to the input service provider
19. Not availing cenvat credits in respect of input services on a timely basis thereby necessitating the payment of taxes in cash

These are some of the errors frequently noted and a deeper analysis would lead to more issues which are quite common especially in each of the individual services.

CHAPTER 17. INTEREST, PENALTY ETC.

Interest and penalty calculations

The Finance Act 1994 has prescribed interest and penal clauses for contravention of any provisions or rules made under the act. No penalty is leviable under sec 76, 77 or 78 if the assessee proves that there was reasonable cause for such failure. The relaxation is provided in sec 80. As per statutory provisions only one penalty can be imposed for delay in taking single registration for more than one taxable service or for delay in filing of return by assessee providing more than one taxable service. Interest payments are mandatory and cannot be waived however penalty can be waived partially. Penalty u/s 76, which is levied for failure to pay tax, cannot exceed the tax payable.

Illustration 1: Mr. Nagabhushan was liable to remit the service tax to the tune of Rs 75000 for the month of March., Mr. Nagabhushan was a tax compliant service provider and he was of the understanding that the due date is 5th of subsequent month and paid the amount by Apr 5th. Later on Mr. Nagabhushan realizes his mistake and wants to pay the interest for delayed portion.

Solution:

Particulars	Amount
Due date for payment	31 st March
Date of Payment	5 th of April
Days of Delay	5
Rate of interest	13%
Amount of interest to be paid	Rs 75000 X 13% X 5/365 = 133/-

Illustration 2: Mr. Prince, service provider fails to pay service tax of Rs 8 lakhs payable by 5th January. Mr. Prince pays it on 20th January. The default has continued for 15 days. Quantify the penalty to be paid by Mr. Prince.

Solution:

Particulars	Amount
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Default in amount	8 lakhs
Days of default	15 days
Penalty (a)	$2\% \times 8 \text{ lakhs} \times 15/31 = 7741$
(b)	$200 \text{ per day} \times 15 \text{ days} = 3000$
Penalty under sec 76 is higher of (a) and (b)	Rs 7741/-

Provisions as to penalty

The provisions as to penalty under service tax are as follows –

- Section 76 – Deals with penalty to pay service tax at Rs. 200 per day of failure or at 2% of such tax per month which ever is higher, from the first day after due date up to the date of actual payment. Penalty however cannot exceed service tax payable.
- Section 78 – Deals with penalty for suppression of value of taxable service and the penalty shall not be less than the service tax and shall not exceed twice the amount of service tax payable. This can be reduced on payment of tax and interest within the stated period of 30 days as explained earlier, along with the penalty determined. (*Where penalty is levied u/s 78, no penalty shall apply u/s 76*)
- Section 77 – Deals with penalty for a contravention where no penalty is prescribed and is shown in table below -

<i>Particulars</i>	<i>Amount of penalty in Rs.</i>
On account of failure to make payment and take registration under service tax	Rs. 200 per day of default or a sum of Rs. 5000 whichever is higher
On account of failure to make electronic payment of tax	Rs. 5000
Failure to maintain proper records or books	Rs. 5000
Failure to furnish information called for under this chapter or Failure to furnish documents required under this chapter or Failure to appear before CEO when issued summons to appear or produce documents in an inquiry	Rs 200 per day of default or a sum of Rs. 5000 which ever is higher
Failure to issue proper invoice or issuing invoice with	Rs. 5000

incorrect or incomplete details or failure to account invoice in books	
Other cases	Rs. 5000

Searching of premises by authorized officers

The Commissioner of Central Excise u/s 82 can authorize any ACCE/DCCE to search for and seize documents or books or things, which have been preserved in any place and which in his opinion would be useful for or relevant to any proceeding under this chapter. He may even take up the task himself. The Code of Criminal Procedure 1973 shall also apply here.

Other recovery provisions

Section 87 of the Finance Act 1994, empowers the Central Excise Officer (CEO) to require any other person or other CEO to deduct the amounts due to the government from the assessee and pay the same. This deduction would be relevant where the person to whom a notice has been issued, owes something to the person who owes money to the government. Where the person to whom a notice is issued does not pay the amount, he himself would be treated as an assessee in default. The CEO can even send a certificate specifying the amount due, to the collector of the district where the person liable to pay resides or has his property. This would be so where the district is different from the one over which the CEO has jurisdiction.

Application of the provisions of the Central Excise Act 1944

The assessee should note that certain provisions of Central Excise Act 1944 would also apply with regard to service tax by virtue of section 83. Thus with regard to these aspects, the aforesaid law would have to be referred. Some of the important aspects with regard to which the provisions of CEA 1994 would apply are as follows –

- Presumption of culpable mental state (Sec 9C)
- Relevancy of statements under certain circumstances (Sec 9D)
- Claim for refund of duty (Sec 11B)
- Interest on delayed refunds (Sec 11BB)
- Power not to recover duty of excise not levied or short-levied as a result of general practice (Sec 11C)
- Declaration of the amount of duty on invoice (Sec 12A)

- Presumption that the incidence of duty has been passed on to the buyer (Sec 12B)
- Crediting of refunds to Consumer Welfare Fund (Sec 12C)
- Power to summon persons to give evidence and produce documents in inquiries under this Act (Sec 14)
- Special audit in cases where credits availed or utilized are not within normal limits (Sec 14AA)
- Procedure for adjudication (Sec 33A)
- Deposit of duty pending appeal (Sec 35F)
- Sections 35FF to 35 –O dealing with AppealsInstruction to officers (Sec. 37B)
- Service of decisions, orders, summons etc (Sec 37C)
- Effect of amendments of rules, notifications etc (Sec 38A)

The professional who advises on service tax should be aware of the implications of the above provisions which maybe judicially clear as they have gone through a number of years of modifications. In case of matters for consultation, the latest position of law maybe confirmed before taking any action. This online book does not propose to be an online treatise/ commentary. The authors only wish to share some of their views which would assist professionals in industry as well as in practice to understand a few concepts.