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Applicability of Service Tax

1) Penalty/Liquidated damages (LD) recovered for non performance of Contract

In every contract whether be it Works contract or Service contract a Clause is inserted for levy of Penalty/LD for non performance of contract to safeguard the interest of employer/Owner.

The recoveries of Penal charges/Liquidated damages from a contractor or service provider for non performance of contract or for reasons whatsoever are in the nature of consideration for tolerating such eventuality. As per Section 66E of the Finance Act 1994, ***"the activity of agreeing to the obligation to refrain from an act or to tolerate an act or a situation or to do an act"*** is a "Declared service" and taxable under the category of "Other taxable services" in the hand of recipient of such penal charges/LD.

2) Amount received on account of "Bond charges" and "Notice Pay"

To discourage job hopping, minimise employee attrition rate or to recover the training & other incidental expenditure incurred for an employee , employer normally insert a clause for "Bond charges/Notice period pay" in the appointment letter issued to the employee. If an employee resigned from the organisation during the contractual period a certain sum as stipulated in the appointment letter is recovered from the resigned employee in the name of for "Bond charges/ Notice period pay"

> In terms of Service tax law ***"the activity of agreeing to the obligation to refrain from an act or to tolerate an act or a situation or to do an act"*** is a "Declared service"

The activity of receiving bond charges/notice pay from the employees for not serving the minimum tenure as per the conditions of bond or terms of employment, as the case may be, is exigible to Service Tax and taxable under the category of "Other taxable services" in the hand of employer. So while recovering "Bond charges" and "Notice Pay" the employer should also recover the amount loading Service tax@15% on Bond charges and Notice pay.

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