2016 (7) TMI 307 - GUJARAT HIGH COURT

COMMISSIONER Versus LARSEN AND TOUBRO LTD

TAX APPEAL NO. 42 of 2013 With TAX APPEAL NO. 43 of 2013

Dated: - 01 July 2016

Judgment / Order

MR. AKIL KURESHI AND MR. A.J. SHASTRI, JJ.

FOR THE APPELLANT : MR YN RAVANI, ADVOCATE

FOR THE OPPONENT : MR PK SAHU WITH MR NITIN K MEHTA, ADVOCATE

ORAL JUDGMENT

(PER : HONOURABLE MR.JUSTICE AKIL KURESHI)

1. These tax appeals have been filed by the department challenging the judgement of Customs, Excise & Service Tax Appellate Tribunal ("CESTAT" for short).

2. Facts are noted from Tax Appeal No.42/2013. At the time of admission of appeal, following substantial questions of law were framed :

> "(I) Whether, against the impugned judgement and order passed by the Customs, Excise & Service Tax Appellate Tribunal, present appeal before this Court would be maintainable or not and/or whether the appeal would lie before the Honble Supreme Court as provided under section 35(L) of the Act?
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> (II) If the Question No.(I) is answered in affirmative and it is held that the appeal would be maintainable before this Court, in that case, to consider the following question :
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> (i) Whether the Honble CESTAT Bench, Ahmedabad has erred in holding that for the purpose of levy of Service Tax, the Respondent and L&TEPC unit as a single legal entity in the fact and circumstances of the case, and hence Respondent is not liable to pay Service Tax?"

3. With regard to question no.1 pertaining to maintainability of the appeals before the High Court, a Division Bench by a detailed judgement dated 25.9.2014 disposed of the question and held that the appeals would be maintainable before the High Court in terms of section 35F of the Central Excise Act, 1994("the Act" for short). The sole surviving question therefore, is whether the Tribunal erred in holding that the respondent was not liable to pay service tax. This question arises in the following background :

4. The respondent is a company registered under the Companies Act and has various units established in the country. One of its units is situated in the Special Economic Zone("SEZ" for short). This Special Economic Zone unit had carried out project management activities including planning and controls, technical support, supply chain management. contracts management, engineering and design and back operations for finance and accounts and human resources functions and such services were availed by

units of assessee situated in Domestic Tariff area("DTA" for short). These were in the nature of business support services and were taxable services under the Finance Act, 1994. The adjudicating authority therefore, issued a show cause notice why service tax on such services provided by the assessee should not be levied with penalty and interest. The assessee opposed such proposal mainly on the ground that one unit of a company cannot provide service to another unit since for providing taxable service, it is necessary that there should be two separate entities. The assessee pressed in service the principle of mutuality and contended that there cannot be any service tax on such activities. The adjudicating authority however, was of the opinion that the SEZ and DTA units of the assessee company were separate and distinct units. He referred to rule 4 of Service Tax Rules, 1994 which refers to registration, subrule(3A) of which provides that where an assessee is providing taxable service of more than one premises or offices and does not have any centralized billing systems or centralized accounting systems, he shall make separate applications for registration in respect of each of such premises or offices. He also referred to subrule(7) of rule 19 of the Special Economic Zones Rules, 2006,(hereinafter referred to as "the Rules of 2006") which provides that if an enterprise is operating both as a Domestic Tariff area unit as well as a Special Economic Zone Unit, it shall have two distinct identities with separate books of accounts, but it shall not be necessary for the Special Economic Zone unit to be a separate legal entity. He recorded that assessee's SEZ and DTA units are maintaining separate books of accounts, are separately and independently registered commercial organisations, have separate manpower, distinct identity, separate objectives and expertise. SEZ unit had raised invoices for covering the charges for providing project management services monthwise and such transactions were recorded in their books. He referred to definition of term "person" in section 2(v) of the Special Economic Zones Act, 2005 which is an inclusive definition and includes within its sweep an individual, a Hindu Undivided Family, a cooperative society, a company or even a proprietary concern or an association of person or body of individuals, a local authority and any agency office or branch owned or controlled by such individual, HUF etc. He was therefore, of the opinion that the respondent assessee had not paid service tax though liable. He also held that the respondent assessee had breached relevant provisions of the Finance Act, 1944. He therefore, ordered recovery of service tax with interest and also imposed penalties.

5. This order was carried in appeal by the assessee before the Tribunal. The Tribunal by the impugned judgement dated 22.10.2010 allowed the appeal and set aside the order of the adjudicating authority. The Tribunal held that SEZ unit and DTA unit of the assessee cannot be considered as separate persons. Merely because they are required to maintain separate books of account in terms of rule 19(7) of the Special Economic Zones Rules, would not mean they are separate entities. The Tribunal was of the opinion that service tax would be levied on a transaction between a person and another person and levy of service tax therefore, would require a transaction between two persons. It is against this judgement that the department has filed the present appeals.

6. Learned counsel for the department contended that the Tribunal committed an error in interpreting the provisions of the Finance Act, 1994. SEZ unit was distinct and separate entity and provided taxable service to DTA unit of the same company. Merely because both the units were under the same company, would not mean that the services provided is not taxable. He submitted that the principle of mutuality would not apply and was wrongly applied by the Tribunal. He invited our attention to rule 19(7) of the Special Economic Zone Rules to contend that SEZ unit is a distinct and separate entity from other units of the same company situated outside the said SEZ area. Counsel relied on decision of Division Bench of this Court in case of **Sintex Industries Ltd. v. Commissioner of Central Excise** reported in 2013(287) ELT 281 in which the assessee had two units within a common boundary wall, having two separate central excise registration. In such background, the Court observed that the assessee having obtained separate registration was

estopped from contending that the two were not separate factories, simply because they were situated within a common boundary wall.

7. On the other hand, learned counsel for the respondent opposed the appeals contending that the assessee company conducted various promotional activities and services for the purpose and benefit of the entire company. Only for convenience, the expenses of services were apportioned to the SEZ unit. In any case, one unit of the company cannot provide any taxable service to another unit. On the principle of mutuality therefore, no service tax can be levied. Counsel relied on the following decisions :

1) In case of **Commr. of Cus. & C. Ex., Meerutl v. Janardan Plywood Industries Ltd.** reported in 2015(323) ELT 46 (Uttarakhand), in which it was found that the company had two manufacturing units. In context of small scale industries exemption, it was held that the manufacturer of both the units is a single legal entity and, therefore, aggregate value of clearances of both the units must be taken into account for determining the eligibility of SSI exemption.

2) In case of **Sahney Steel and Press works Limited and another v. Commercial Tax Officer and others** reported in (1985) 4 Supreme Court Cases 173, in which in the context of Sales Tax Act, it was noticed that the manufacturer had sent goods to the branch office for supplying to the buyer. It was observed that in such a case the branch office merely acted as a conduit through which the goods passed on their way to the buyer. Both the registered office and the branch office are offices of the same company and that what in effect did take place was that the company from its registered office in Hyderabad took the goods to its branch office outside the State and arranged to deliver them to the buyer.

3) In case of **UP State Cement Corporation Ltd. v. Commissioner of Sales Tax, UP** reported in 1979 (43) STC 475 (ALL), it was noticed that UP Government owned two cement factories. One supplied cement to another for which it was also billed. In context of liability to pay sales tax, it was observed that before a transaction can be taxed and included in the turnover of a dealer, it has to be a sale. In order to constitute sales within the definition of Sales Tax Act, there must be two different persons in the ordinary sense of the term 'person'.

4) In case of **Commissioner of Incometax v. Prabhukunj Coop Housing Society Ltd.** reported in 377 ITR 13 (Guj), in which the principle of mutuality, the members of a cooperative housing society and its members, was applied in the context of a part of the surplus retained by the society from the sale of a plot by its member.

8. Having heard learned counsel for the parties and having perused the materials on record, we may refer to the relevant statutory provisions. Section 66 of the Finance Act,1994 pertains to charge of service tax and provides that there shall be levied a tax referred to as the service tax at the rate of 12 per cent of the value of taxable services referred in clauses (a) to (zzzzw) in subsection(105) of section 65 and collected in such manner as may be prescribed. Section 65(105) defines various taxable services. Clause (zzzq) thereof pertains to service provided to any person by any other person in relation to support services of business or commerce in any manner. Section 65(104c) defines support services of business or commerce as under :

"Support Services of Business or Commerce" means services provided in relation to business or commerce and includes evaluation of prospective customers, telemarketing, processing of purchase orders and fulfilment services, information and tracking of delivery schedules, managing distribution and logistics, customer relationship management services, accounting and processing of transactions, [operational or administrative assistance in any manner], formulation of customer

service and pricing policies, infrastructural support services and other transaction processing.

Explanation For the purposes of this clause, the expression "infrastructural support services" includes providing office along with office utilities, lounge, reception with competent personnel to handle messages, secretarial services, internet and telecom facilities, pantry and security;

9. In terms of these provisions, therefore, in ordinary circumstances, it is not even the case of the respondent that the services provided by the SEZ unit not in the nature of support services of business or that for any other reason, they are not taxable services.

10. Section 2(za) of the Special Economic Zones Act, 2005 defines Special Economic Zone as to mean a Special Economic Zone notified under the proviso to subsection(4) of section 3 and subsection(1) of section 4. Section 2(zc) defines unit to mean a unit set up by an entrepreneur in a Special Economic Zone and would include an existing unit. Section 7 of the Special Economic Zones Act, 2005 pertains to exemption from taxes, duties or cess and provides that any goods or services exported out of, or imported into, or procured from the Domestic Tariff Area by a unit in a Special Economic Zone or a developer, shall subject to such terms, conditions and limitations as may be prescribed, be exempt from the payment of taxes, duties or cess under all enactments specified in the First Schedule. Section 30 of the Special Economic Zones Act, 2005 reads as under :

“Domestic clearance by Units.-Subject to the conditions specified in the rules made by the Central Government in this behalf:-

(a) any goods removed from a Special Economic Zone to the Domestic Tariff Area shall be chargeable to duties of customs including antidumping, countervailing and safeguard duties under the Customs Tariff Act, 1975 (51 of 1975), where applicable, as leviable on such goods when imported; and

(b) the rate of duty and tariff valuation, if any, applicable to goods removed from a Special Economic Zone shall be at the rate and tariff valuation in force as on the date of such removal, and where such date is not ascertainable, on the date of payment of duty.”

11. Under section 30 of this Act, therefore, any goods removed from a Special Economic Zone to the Domestic Tariff Area would be chargeable to duties of customs including antidumping, countervailing and safeguard duties under the Customs Tariff Act, as leviable on such goods when imported.

12. In exercise of powers conferred under the Special Economic Zones Act, 2005, the Central Government has framed the Special Economic Zones Rules, 2006. Rule 19 thereof pertains to letter of approval to a unit and provides for various details that the letter of approval granted to a unit of manufacturing specified project in the SEZ units. Subrule(7) thereof reads as under :

“(7) If an enterprise is operating both as a Domestic Tariff Area unit as well as a Special Economic Zone Unit, it shall have two distinct identities with separate books of accounts, but it shall not be necessary for the Special Economic Zone unit to be a separate legal entity:

Provided that foreign companies can also set up manufacturing units as their branch operations in the Special Economic Zones in accordance with the provisions of Foreign Exchange Management (Establishment in India of branch or office or other place of business) Regulations, 2000 as amended from time to time.”

13. Rule 22 of the Rules of 2006 pertains to terms and conditions for availing exemptions, drawbacks and concessions to every developer and entrepreneur for authorised operations. Subrules (2) and (3) read as

under :

> "(2) Every Unit and Developer shall maintain proper accounts, financial yearwise, and such accounts which should clearly indicate in value terms the goods imported or procured from Domestic Tariff Area, consumption or utilization of goods, production of goods, including byproducts, waste or scrap or remnants, disposal of goods manufactured or produced, by way of exports, sales or supplies in the domestic tariff area or transfer to Special Economic Zone or Export Oriented Unit or Electronic Hardware Technology Park or Software Technology Park Units or Biotechnology Park Unit, as the case may be, and balance in stock:
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> Provided that unit and developer shall maintain such records for a period of seven years from the end of relevant financial year:
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> Provided further that the unit engaged in both trading and manufacturing activities shall maintain separate records for trading and manufacturing activities.
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> (3) The Unit shall submit Annual Performance Reports in the Form I, to the Development Commissioner and the Development Commissioner shall place the same before the Approval Committee for consideration.
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> 01.07.2016

14. From these statutory provisions, it can be seen that upon the support services of business being provided by a service provider, service tax at the prescribed rates would be levied. In view of materials on record, we have proceeded on the basis that the respondent company SEZ unit had provided such services to its DTA unit. We may notice that the Special Economic Zones Act was enacted to provide for the establishment, development and management of the Special Economic Zones for the promotion of exports and for matters connected therewith or incidental thereto. This Act makes special provisions for the units situated in Special Economic Zones to be notified and established. Under section 7 of the Special Economic Zones Act, 2005, any goods or services exported out of, or imported into, or procured from the Domestic Tariff Area by a unit in a Special Economic Zone or a developer, would be subject to such terms and conditions as may be prescribed, exempt from the payment of taxes, duties or cess under all enactments specified in the First Schedule. Thus, for the purpose of taxation of various kinds within the unit situated in the Special Economic Zones, receive a special consideration. It is because of these concessions granted to such units that under section 30 of the Special Economic Zones Act, 2005, it is provided that in cases of goods removed from a Special Economic Zone to the Domestic Tariff Area, the same would be chargeable to duties of customs including antidumping, countervailing and safeguard duties under the Customs Tariff Act, as applicable, leviable on such goods when imported. In view of such special status and in order to enable a unit to claim such exemption, drawbacks and concession, under subrule(2) of Rule 22 of the Special Economic Zones Rules, 2006, it is provided that every unit and developer has to maintain proper accounts financial yearwise, clearly indicating in value terms the goods imported or procured from Domestic Tariff Area, consumption or utilization of goods, production of goods,etc. Under subrule(3), a unit would have to submit Annual Performance Reports which shall have to be placed before the Approval Committee for consideration. Likewise, under subrule(7) of Rule 19 it is provided that if an enterprise is operating both Domestic Tariff Area unit as well as a Special Economic Zone Unit, it shall have two distinct identities with separate books of accounts, but it shall not be necessary for the Special Economic Zone unit to be a separate legal entity.

15. All these statutory provisions indicate separate and artificially created independent existence of a SEZ unit of a company whether it has another unit situated in Domestic Tariff Area or not. In particular, Rule

19(7) of the Special Economic Zones Rules, 2006 while recognising that the same legal entity may have two units, one in SEZ and another in DTA, mandates that the two would have distinct identities with separate books of accounts. It is because of the special concessions in taxation, including duty drawbacks and other exemptions that the SEZ unit has to maintain scrupulously accounts of all imports and procurements from Domestic Tariff Area. It also has to pay customs duty on goods cleared to Domestic Tariff areas as if such goods were imported into India. Subrule(7) of Rule 19 clarifies that in case of an enterprise which has unit both situated in SEZ as well as in Domestic Tariff Area, the two would have distinct identities with separate books of accounts, but it would not be necessary for the Special Economic Zone unit to be a separate legal entity.

16. For various purposes, thus a SEZ unit of an enterprise which also has an additional unit in Domestic Tariff Area, therefore, has a distinct identity. Its accounts are separate, its accounting would be separate. This artificial creation of separate accounting of a unit or an industry of a common enterprise or a company, is not a new or unknown phenomena. In number of cases, where Income Tax Act provides profit linked incentives such as deductions under sections 80HHC, 80I, 80IA, 80IB, etc., the industry or unit engaged in such eligible business is treated separate and distinct for the purpose of accounting so that deductions of the assessee out of its eligible business can be separately worked out. Similar principles would apply in other special deductions also whether area based or investment based. It may be that while assessing the company, its total income would have to be computed and the income of the assessee from such eligible business after deductions, would also form part of the total income. Nevertheless, for the purpose of accounting, the particular industry eligible for deduction would be treated separate from other units.

17. Under the circumstances, in view of statutory scheme noticed in the Finance Act, 1994 and Special Economic Zones Act, 2005, the contention of the respondent company that on the principle of mutuality, the services rendered by its SEZ unit to a Domestic Tariff Area unit, would not be chargeable to service tax, cannot be accepted. If this principle is applied, the very artificial creation of treating a SEZ unit separate and distinct for accounting, consumption of raw materials, production and clearance purposes would shatter. The concept of mutuality is essentially based on the principle that where certain services or facilities are created by group of persons for themselves, as in the case of a club for recreation, any excess or residue, from out of the funds collected, would not become the income of the club chargeable to tax.

18. The question of charging service tax however, needs to be looked from a slightly different angle. Section 66 of the Finance Act, 1994, as noted, provides for levy of taxes at the rate of prescribed percentage of the value of taxable services referred to in various clauses of subsection(105) of Section 65. For applicability of this charging section, therefore, what is needed is to ascertain the value of taxable service. In other words, service tax can be levied only if the service is provided, even if it is otherwise, a taxable service, carries a certain value. If the value of service provided is nil, there would be no occasion for charging the service tax. In essence, thus section 66 aims at collecting service tax when a certain service is provided for a value. To put it conversely, when the service is provided but no value thereof is charged, there would be no question of collecting service tax. No provision has been brought to our notice in the Finance Act, 1994 under which though the service provider has not charged any value for service, service tax thereon still can be levied on its deemed value, be it market value or fair value. It is a different matter altogether if the departmental authority disbelieves that though service was provided but no charge was collected and in such a case, the authority would have ample power to inquire into the matter and come to appropriate conclusion on the basis of available materials on record. However, if the department proceeds on the premise that a certain service though otherwise a taxable service, the service provider did not collect any charge for the same from the service recipient, in our opinion, it would simply not be possible for the authority to collect any service tax on such service.

19. We may notice that explanation to section 65 states as under :

> “For the purposes of this section, taxable service includes any taxable service provided or to be provided by any unincorporated association or body of persons, to a member thereof, for cash, deferred payment or any other valuable consideration.”

20. Thus the term taxable service has a direct relation to the consideration either paid in cash or by way of deferred payment or by mentioning of any other valuable consideration. This would reinforce our belief that when no charge was collected for providing the service, there would be no question of applying a rate of tax on the value of such service.

21. In this context, we may recall, according to the assessee, providing of service by its SEZ unit to its DTA unit was merely for the purpose of convenience and SEZ unit had not collected any charge for such service from its DTA unit. Though the Assessing Officer in his order has made a brief reference to the SEZ unit receiving consideration for such service, we do not find any basis for such a conclusion. In fact, the case of assessee all along has been that invoices were raised for such services merely for the purpose of convenience and in fact, since promotional programmes were being organised, which would benefit the entire company and its different units, there was no question of charging a particular unit by SEZ unit for such service and that raising of invoices was merely for the purpose of convenience. If that be so, in our opinion, no service tax could be levied not on the principle of mutuality but, as noted, on the ground that service provided carried no actual value.

22. For such reasons, while therefore, dismissing the Revenue's appeal against the judgement of the Tribunal, on the grounds different from which appealed to the Tribunal, we answer the question clarifying that in the present case, no service tax was leviable since the SEZ unit of respondent assessee had not charged for the services provided to its DTA unit.

23. Tax appeals are dismissed.

Citations: in 2016 (7) TMI 307 - GUJARAT HIGH COURT

1. Sahney Steel and Press Works Ltd. and Another Versus Commercial Tax Officer and Others - 1985 (9) TMI 313 - SUPREME COURT OF INDIA
2. Commissioner, Customs and Central Excise, Meerut-I Versus M/s Janardan Plywood Industries Ltd., Dehradun - 2015 (9) TMI 690 - UTTARAKHAND HIGH COURT
3. COMMISSIONER OF INCOME-TAX Versus PRABHUKUNJ CO-OP. HOUSING SOCIETY LIMITED - 2015 (7) TMI 877 - GUJARAT HIGH COURT
4. SINTEX INDUSTRIES LTD. Versus COMMISSIONER OF CENTRAL EXCISE - 2013 (6) TMI 178 - GUJARAT HIGH COURT
5. UP. State Cement Corporation Ltd. Versus Commissioner of Sales Tax, UP. - 1978 (8) TMI 202 - ALLAHABAD HIGH COURT