

Service Tax on Renting Services – where is the ‘Lessor’s Alternative?’ – Oct 11, 2011

I was greatly inspired by the thriller ‘The Devil’s Alternative’ that the great Frederick Forsyth wrote, in the backdrop of the then existing superpower, the Soviet Union, in the 1980s. I remember finishing this book in one go, foregoing my sleep for a couple of days. In effect, this thriller talks of an alternative that does not simply exist.... a situation, similar to choosing between the devil and the deep blue sea, perhaps.

The situation, in so far, as the thriller related to the levy of service tax on renting services is concerned, is no different. In this ‘tax thriller’, there seems to be no practical alternative that is available to the Landlords/Lessors, as they are caught between one High Court after another upholding the constitutional validity of the service tax levy and their tenants (read, Retail Players) still refusing to pay service tax citing that the case is before the Supreme Court.

Even as the Larger Bench of the Delhi High Court upheld the levy of service tax on renting of immovable property services and even the retrospectivity of the levy, a few days back, I for one, had thought, that this was the end of litigation on this subject matter. Of course, I had been forewarned by my learned Advocate friend, Mr. Rakesh Chitkara, not to expect any pleasant surprises from the Delhi High Court, especially after the other High Courts of P & H, Gujarat and Bombay, had upheld the levy on a retrospective basis. Now comes the news that the Apex Court has admitted the SLP filed against the decision of the Bombay High Court and has stayed the collection of service tax for the period up to September 30, 2011 and has posted further hearings to October 14. The matter has come one full circle time and it’s perhaps, time, to pause and take a look...

What could be the outcome of the SLP filed with the Apex Court? And, if takes several years for a decision to come out from the Apex Court, how could things work out, in the meantime?

As far as my understanding goes, the stay of the Apex Court could work qua the decision of the Bombay High Court and this stay may not apply to cases not falling under the jurisdiction of the Bombay High Court.

Notwithstanding this, I, for one, have always taken the view that, the levy would ultimately get upheld in the judicial forums, even when the Delhi High Court had given a stay, in the first Home Solutions case. With four High Courts having upheld the levy on a retrospective basis, it remains to be seen if the Apex Court would indeed make a departure and strike down the service tax levy. On the other hand, if it upholds the levy (which, I guess, it will), the question is, whether the levy would be upheld on a retrospective basis? My guess here is as good, as anybody else’s.

Even if the Apex Court strikes down the levy, it would not prevent the Central Government from going for another round of statutory amendments to overcome the Apex Court’s decision.

Assuming that the Apex Court upholds the levy; would penalties be Levi able by the Department? Not, in my view, as the matter could be said to have attained finality only on the Apex Court delivering the final decision.

And, how about interest, Sir, for the delayed payment of service tax? In my view, since there is no provision in the service tax law to waive the levy of interest, this is not a matter which even the Apex Court can decide. Of course, there are precedents wherein, the Apex Court has intervened for waiving interest, but in this case, this may not happen, as there is no statutory provision for waiver of interest.

And, in the event that the Supreme Court strikes down the service tax levy on renting services, what could happen to the tens of hundreds of crores of rupees which have already been collected by the Government?

Perhaps, the doctrine of prospective overruling could get invoked, resulting in the forfeiture of the amounts already collected as tax.

The litigation on this subject matter has been completely driven by the Retail Lobby, as we all know. None of the non-retail tenants, whom I know of, have refused to pay service tax to their Lessors. The plight of the Retail Players is understandable, in as much as, they have no means to avail of cenvat credit, of the service tax paid on rentals, which forms a significant portion of their overall cost of operations.

But, can the Retail Players hold their Lessors/Landlords to ransom, by refusing to pay service tax on the premise that the matter is yet to attain finality in view of the Apex Court having admitted the petition against the Bombay High Court's order?

Of course, not, from a legal perspective. The Retail Players have, in fact, no locus standi, to challenge the constitutional validity of the service tax on renting services, when the levy is actually on the Landlords/Lessors. The Karnataka High Court has already held while dismissing certain writ petitions filed by the tenants, that, the 'tenant' being not a service provider, cannot question the levy of service tax on renting services and hence, any writ filed by the tenant, questioning the constitutional validity of the service tax levy on renting services, is not maintainable. I would wish that this point is brought to the notice of the Hon'ble Apex Court, by the Government Counsel.

Where does the current situation leave the Lessors/Landlords?

Of course, as the title suggests, with no alternative.

While, they continue to be under the hanging sword of being asked to pay service tax along with interest, their tenants could continue to refuse to pay service tax, citing the recent developments in the Apex Court.

Here are some practical suggestions for the Landlords/Lessors:

They should make all efforts to discharge their own service tax liability in respect of renting services, along with interest. Of course, they would be strongly advised to utilize the cenvat credit that could have accrued to them, up to March 31, 2011. Of course, while Landlords/Lessors are not allowed to avail of cenvat credit of the service tax paid on input commercial construction services with effect from April 1, 2011, due to an amendment in the definition of 'input services' covered under the Cenvat Credit Rules, 2004, there is no bar on the utilization of the cenvat credit availed on or before March 31, 2011, for payment of service tax on renting services post March 31, 2011. Further, in my strong view, Circular No. 98/1/2008-ST dated January 4, 2008, which talks of denial of cenvat credit of the service tax paid on input commercial construction services, vis-à-vis renting services being the output service, is very unlikely to stand judicial scrutiny.

Of course, all out efforts are required to be made by the Landlords/Tenants to collect the service tax from their tenants, even if there is no specific mention of service tax in the tenancy/lease agreements. They would do well to bear in mind, the decision of the Delhi High Court, in *Pearey Lal Bhawan Association Vs M/s Satya Developers Pvt Ltd* reported in [2011-TIOL-114-HC-DEL-ST](#), to the effect that, with specific reference to the service tax levy on renting of immovable property services, the tenant is required to pay the service tax to the service provider even if the contract did not specifically mention it.

Landlords/Lessors would also be advised to keep in mind the fact that, under the Limitation Act of 2005, no civil suit for recovery of amounts covered by contracts, can be instituted beyond a period of 3 years and this could apply to the recovery of service tax amounts by from the tenants, by the landlords and lessors, as well.

The period has been prescribed in Schedule to the Act. Generally, it is as follows – (a) 3 years for a suit relating to accounts, contracts, declarations, decrees, suits relating to movable property, recovery of law suit under a contract etc.

Before concluding...

One would wonder as to, how the various High Courts entertained the writ petitions filed by the Retail Lobby and their Associations challenging the constitutional validity of the service tax levy on renting services, in the first place and did not dismiss these writs, on grounds of non-maintainability, as was very rightly done by the Karnataka High Court.

If this had been done, this subject matter would not have seen this much of litigation, after all. And, I would have had to refer to Frederick Forsyth.

TIOL's Editor-In-Chief, in his DDT column, had rather sarcastically mentioned that an Under Secretary in the Board has the powers to undo the orders of the Apex Court of the country. I couldn't, but agree.

Lastly..... why can't the Government think of exempting lease of commercial properties for the Retail Sector, Home Theaters, etc. from the levy of service tax? After all, these players have no way of availing credit of the service tax paid on rentals, as contrasted to the other players. This would not only be just, but also be a wise move from the Government, which can bring the whole issue related to the levy of service tax on renting services to a logical end.