

Service Tax on Restaurants and Hotels – Centre transgressing into States' territory – Feb 28, 2011

THE Finance Minister has proposed to levy service tax on Restaurants and Hotels, Inns, etc. In terms of the Finance Bill, a new clause (zzzzv) is proposed to be added to Section 65(105) of the Finance Act, 1994, in terms of which, services provided by a restaurant is proposed to be brought into the service tax net. The definition of the new taxable service, reads as follows:

“to any person, by a restaurant, by whatever name called, having the facility of air-conditioning in any part of the establishment, at any time during the financial year, which has license to serve alcoholic beverages in relation to serving of food or beverages, including alcoholic beverages, including alcoholic beverages or both, in its premises”.

The customary post Budget circular, issued by the TRU, makes a very interesting reading and the following conclusions could emerge ...

The Central Government is seeking to levy service tax on, what are essentially, sale of meals/beverages, etc., and/or on the charges for the use of movable assets like furniture, linen, cutlery, crockery, etc. These are activities which are clearly considered as 'sale' within the meaning of the VAT law and are accordingly subjected to the levy of VAT. How can transactions, which are 'sales' even by the own admission of the Government, as reflected in its Circular, with certain inherent services, be subjected to service tax.

The definition states that restaurants which have the facility of air-conditioning in any part of the establishment at any time during the financial year, which has license to sell alcoholic beverages would be subjected to the service tax levy. The TRU circular further states that the levy is directed at services provided by high-end restaurants that are air-conditioned and have license to liquor. The whole rationale behind this levy seems extremely flawed.

For instance ... if a restaurant is to get an air-conditioning facility, let's assume, on March 1, how on earth can it be required to pay service tax from April 1 of the financial year. How will the restaurant ever be able to go back and collect service tax for the back period?

To treat a value added sale as a service is an obnoxious development. So, is the attempt to deem a restaurant having an air-conditioning facility, in any part of the premises, as a service provider? Is a restaurant, whose owner's room is air-conditioned, also to be treated as providing services, in respect of the dining room?

Though an abatement of 70% is provided, the fact remains that, 100% of the most of the items sold by a restaurant including food and non-alcoholic beverages are subjected to the VAT levy and to this extent, the levy of service tax would result in a double levy.

In terms of the Clause (zzzzw) of Section 65(105), as proposed, service tax is proposed to be levied on hotels, inns, guest houses, clubs and others and at camp-sites, where the stay is for a continuous period of less than 3 months. Room rentals are charged to luxury tax. The levy of service tax on room rentals, would result in a double levy, on the same transaction. Given the fact that it is difficult to find short term accommodation at hotels, etc. for less than Rs 1,000- per day, the levy of service tax is bound to increase the overall cost of hotel stay, etc.

The TRU circular states that, the actual levy would be restricted to accommodation with declared tariff of Rs 1,000- per day or higher by an exemption notification and that, once this requirement is met, service tax will be chargeable irrespective of the fact that the actual amount charged from a particular customer is less than

Rs 1,000/-. Here again, one finds an attempt to levy service tax on a notional basis. Despite the Government has proposing to give a 50% abatement, there can be no doubt that the same transaction would get subjected to the levy of luxury tax and service tax.

It is not clear whether, cenvat credit would be available for these service providers, given the fact that, they would be able to take the benefit of abatement.

The proposal to levy service tax on transactions, which are already subject to the sales tax and luxury tax levies, is an attempt by the Centre to transgress into the tax territory reserved for the States.