Service Tax refunds to exporters… Back to 'Square One' after Bangalore Tribunal Decision – Apr 27, 2010

Service Tax refunds to exporters… Back to 'Square One' after Bangalore Tribunal Decision

APRIL 27, 2010

By S Sivakumar, CA

WRITING in **TIOL** earlier, I had warned that the ***Circular No. 120/01/2010-ST dated January 19, 2010*** and the proposed amendment to ***Notification No. 5/2006-CE dated 14-3-2006*** are unlikely to make any great impact, in terms of refund of service tax credit to exporters, unless and until the all important Rule 5 of the Cenvat Credit Rules, 2004 and other statutory provisions were amended. As we know, t he Government is proposing to add, retrospectively with effect from 14-3-2006, the words " in relation to " in the main condition (a) of the Notification. There is also a proposal to replace the word "in" contained in main condition (b) of the said Notification, with the word "for". As per the Board Circular No . D.O.F. No.334/1/2010-TRU dated 26-2-2010, t he above two changes would ensure that the provisions of the refund notification and the CENVAT Credit Rules are aligned and that refund is granted on all goods or services on which *CENVAT* can be claimed by the exporter of goods or services. So much, for theory.

On the practical side, my worst fear that these amendments would have little practical impact, without an amendment to Rule 5 of the CCR stands confirmed, post the decision of the Bangalore Tribunal in the Kbace Tech Pvt Ltd case covered by Appeal No. ST/304/09, dated March 19, 2010. The operative parts of this very important decision are reproduced below:

Quote :

We have considered the submissions made from both sides well as the case records, the cited case laws and the Circular dated 19.01.10. We note at the outset that all these appeals relate to case of export made by export oriented units. We also note the anxiety of the Government as reflected in the Circular dated 19.01.10, that the Government wants to refund the accumulated input credit to the exporters and zero-rate the exports.

In the said circular, note has been taken regarding use different phrases in the relevant rules and notifications. In addition, we find that the expression used in the Act is also different pointed out in para-6 above, the legislature uses the expression services consumed under Section 94 (ee) and (eee). The rules made taking recourse to the statutory provisions contained in the Act the notifications issued there under have to be interpreted the notifications issued there under have to be interpreted in the context of the expression used in the Act.

All the rules of procedure are the handmaid of justice as held in *Kailash v. Nanku – AIR 2005 SC 2441*. In the *State of Punjab and another v. Shamala Murari and another, (1976) 1 SCC 719,* Apex Court approved in no unmistakable terms the approach of moderating into wholesome directions what is regarded as mandatory on the principle that Procedural law is not to be a tyrant but a servant, not an obstruction but an aid to justice. Procedural prescriptions are the handmaid and not the mistress, a lubricant, not a resistant in the administration of justice. In *Ghanshyam Dass and others V. Dominion of India and others (1984) 3 SCC 46*, the Court reiterated-the need for. interpreting a part of the adjective law dealing with procedure alone in such a manner as to sub-serve and advance the cause of justice rather than to defeat it as all the laws of procedure are based on this principle. It is settled principles of law that the courts when called upon to interpret the nature of the provision, may keeping in view the entire context in which the provision came to be enacted, hold the same to be directory though worded in the negative form.

Language employed in subordinate legislation alone most often is not decisive, but regard must be had to the extent, subject-matter and object of the statutory provision in question, indetermining whether the same is consonance with legislative mandate. No rule can be laid down as to whether mandatory enactments shall be considered directory only or obligatory with an implied nullification for disobedience to the statutory provision. It is the duty of Courts of Justice to try to get at the real intention of the Legislature by carefully attending to the whole scope of the statute to be considered. For ascertaining the real intention of the Legislature / the court may consider inter alia, the nature and design of the statute, and the consequences which would follow from construing it the one way or the other; the impact of other

provisions whereby the necessity of complying with the provisions in question is avoided; the circumstances, namely, that the statute provides for a contingency of the non-compliance with the provisions; the fact that the noncompliance with the provisions is or is not visited by some penalty; the serious or the trivial consequence, that flow therefrom; and above all, whether the object of the legislation will be defeated or furthered. Rule cannot be interpreted de hors the legislation and particularly in fiscal jurisprudence if Rule departs from legislative intent that may cause peril to public revenue.

We find that as a part of the Budget proposal this year some amendments have been made. ***Notification No. 5/06-CE(NT) dated 14.03.06***, issued under Rule 5 of the Cenvat Credit Rules, 2004, has been retrospectively amended as follows:-

- *The words "in relation to" have been added in main | condition (a) of the Notification.*
- *The word "in' contained in main condition (b) of the said Notification has been respected with "for".*
- *The illustration given in condition 5 of the Appendix to the Notification has been deleted.*

We, however, find that neither the Act, nor the Rules have been retrospectively amended.

Some prospective amendments have also been made to the said ***Notification No. 5/06-CE(NT) dated 14.3.06***, requiring certification of details relating to refund claim including certification by a Chartered Accountant.
These changes, do not alter the fact that the expression used in the Finance Act, 1994, speaks of services consumed for providing a taxable service and the expressions used in the Cenvat Credit Rules, 2004 and in the Notification issued there under are different. The Rules and Notifications issued under the enabling power under the Act cannot expand the mandate given under the enactment and cannot make provision for allowing credit in excess of what is stipulated under the law. The rule making authority can frame rules covering a lesser area than what it is empowered to do but cannot go beyond the limits provided under the statute and make rules covering a greater area,

While we fully appreciate and support the idea that the refunds in respect of unutilized and accumulated credit should be sanctioned to the exporters as expeditiously as possible, without any delay, no refund can be granted under the rules and the notifications in respect of services other than the services consumed for providing output service in view of the express language used in the statute. The Board's Circular dated 19.01.10 cited before us does not have the effect of amending the statute and cannot be seen as authorizing sanction of refund if the credit of service tax does not relate to services consumed for providing the output service. The officials sanctioning refund have to, therefore ; necessarily examine if the credit relates to services consumed for providing the output service in view of the statutory provision unless the statute is amended.

In the course of hearing of these appeals, both sides confirmed that since the appellants are export oriented units and are exporting the services, no examination has been done at the time the credit has been taken as to whether such credit is admissible in terms of the statutory provision and the rules and notifications made thereunder. It was argued before us that in the case of CST Delhi Vs. Converges India Pvt. Ltd. (supra), it has been held that there cannot be two different yard sticks, one for permitting credit and the other for eligibility for granting rebate and that whatever credit has been permitted to be taken, the same should be permitted to be utilized and if such utilization is not possible, refund or rebate should be granted. We entirely agree with the said decision that whatever credit has been permitted to be taken, the same should be permitted to be utilized and if that is not possible, refund or rebate should be granted in case of export of output services. However, in these cases, it was clearly admitted by both sides that initially the credit was taken-by the appellant exporters on their own and the admissibility of such credit ' was not examined by the field officials at that stage since there was no duty payment involved on the output service exported and therefore, no assessments were made. Accordingly, we hold that before granting refund the field officials will be at liberty to verify the admissibility of the credit.

Unquote :

Though, on the face of it, it would seem to a lay person like me that, the Hon'ble Tribunal has held that *Circular No. 102/01/2010*cannot give a benefit which is not contemplated by the statutory provisions contained in Rule 5 of the CCR, a deeper reading of this decision actually points out to the contrary, in as much as, the Tribunal has clearly concurred

with the decision in the Convergys case, wherein it had held that there cannot be two different yardsticks, one for permitting credit and another for refund of the unutilized credit. It seems that this decision of the Bangalore Tribunal has more to do with the process to be undertaken at the level of the Adjudication/Field Officers to ascertain the nature of the input services, etc. , which in any case, is a routine exercise to be undertaken. By the way, the *Circular No. 102/01/2010* never states that the Departmental officers are bound by the statutory/internal auditor certified information submitted by the refund claiming exporter. In fact, the Circular goes to list down some input services, which cannot be considered for purposes of refund of unutilized cenvat credit.

Be that as it may… this decision could aid the Service Tax Department and especially its Adjudicating Officers, who have been working very hard in finding ingenious ways to deny refunds, despite ***Circular No. 120/01/2010***. To some extent, it can be said that the issue related to granting of refund of service tax on input services, is now back to Square One, post this decision. The Department would now be emboldened to continue to take the view that most input services, other than the three or four services, cannot be considered as having been 'used' in the rendering of the services exported and consequently, refund is to be denied.

Most Commissionerates had taken the view, prior to the issuance of the ***Circular No. 120/01/2010*** that, only three or four services can be considered as having been 'used' for providing Information Technology Software Services and have been rejecting refund claims, in respect of the service tax paid on the other input services.

Exporters have to consider themselves lucky that this decision has come now, even when the Finance Bill 2010 is already before the Parliament. The Government, on this side, should take note of this decision and go in for a retrospective amendment to Rule 5 of the CCR, with effect from 14-03-2006 to provide for refund of service tax paid on input services, which are used in or in relation to output services or manufactured goods, which are exported. If this opportunity to move for an amendment to Rule 5 of the CCR is missed now, exporters might have to wait for one more year for a statutory amendment and a lot of water would have flowed down the bridge, for sure.

Before parting…

I've never quite understood the logic of issuing one circular after another and going in for a retrospective amendment to a notification, without amending the all important Rule 5, in so far as it concerns the refund of service tax to exporters. This tamasha of the Government 'trying' to do something positive thro' circulars and notifications and the Department doing the exact reverse how now got to be stopped, Sir. If the Government is indeed serious about addressing the plight of the exporters, it must now act by going in for retrospective amendments to the statutory provisions.

Notwithstanding this, with due respects, I feel that the Tribunal is duty bound to presume and accept the legal validity of the statutory provisions. In this decision, the Tribunal is almost getting into challenging the constitutional validity of the statutory provisions, which is not allowed in terms of various binding decisions of the Apex Court including in *Dhulbhai v. State of MP 22 STC 416, K S Venkataraman v State of Madras (1966) 60 ITR 112 and West Bengal Electricity Regulatory Commission v. CESC Ltd 2002 (8) SCC 715.*

Notwithstanding this Tribunal decision, I would continue to believe that the ***Circular No. 120/01/2010*** is still binding on the Department and its Adjudicating Officers, in terms of the processing of refund applications filed by exporters, as the Bangalore Tribunal has clearly recorded that it is concurring with the Convergys decision, as aforesaid.

Of course, retrospective amendments to the statutory provisions would be required, as aforesaid, including amendments to Rules 2(l) and 5 of the CCR and more importantly, to Section 94(2) of the Finance Act, 1994. The entire cenvat credit rules are based on the authority derived from Section 94(2). The Bangalore Tribunal decision clearly points out to the anomaly arising out of the usage of the word 'consumption' in Section 94(2), as contrasted to the CCR and the Circulars and Notifications issued under Rule 5. Unless and until, a retrospective amendment is carried out to Section 94(2) with effect from September 10, 2004, along with the other amendments suggested, the refund related issues are unlikely to subside.

The ball then, is squarely in the Government's court.