

Why Litigation will necessarily increase under New ST law – June 6, 2012

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158. At the end of June this year, this tax will attain adulthood by completing 18 years. It is therefore time to shift gears and accelerate ahead. However, service tax needs to confront two important challenges to sustain the journey.

These are:

The share of services in taxes remains far below its potential. There is a need to widen the tax base and strengthen its enforcement;

Service Tax law is complex and sometimes avoidably different from Central Excise. We need to bring the two as close as possible in the light of our eventual goal of transition to GST.

Excerpts from Hon'ble FM's Budget 2012 speech...

Nobody has any issues when the FM says that, there is a need to widen the service tax base. However, one is scared when the FM says that, there is a need to bring service tax, which has just attained adulthood, as per him, 'as close and possible' with central excise duty, which we know is a 68 year old law. Since the FM referred to the service tax attaining 'adulthood', I presume that, he was probably equating service tax with a beautiful girl of 18 years, attaining adulthood.... by, implication then, he was referring to central excise duty as a 68 year old man... In effect, he was perhaps, talking of a 68 year old willy old guy and a bright, young and modern 18 year old girl, 'coming together'....

The results will be for everyone to see, perhaps.....

The service tax, from a 'positive' law is now becoming a 'negative' law, in as much as, instead of looking to fit an activity into any of the 120 odd services, one would only have to look at the negative list...anything that is not in the negative list, would fit into the definition of 'service'. Anything and everything, to repeat, which does not fall under the so called negative list and the list of services exempted thro' Notifications, would now become a taxable service.

Most of the two or three volume books available in the market, on service tax, would now become irrelevant, I'm afraid. Of course, the book sellers who bring out as many as three or four editions in a year, would stand to lose a lot, as the so called 'service tax law' would become a rather simple piece of literature, as most activities would come under the new definition of 'service' in terms of the new law.....

Will this so called 'simple' service tax law result in reduced issues, vis-à-vis the Department? Before venturing into this question, let me share my thoughts, on the current status of litigation on service tax..... In the 80s and mid 90s, it was the customs law which saw a lot of litigation. Perhaps, 60% to 70% of the appeals filed then with the CEGAT benches pertained to customs cases, while the balance of the cases related to central excise duty, with a small percentage pertaining to gold related cases. With a progressive reduction in the peak customs duty rates, a process started by an admirably efficient then FM, Dr Manmohan Singh, litigation related to customs started drastically coming down and today, there is hardly any litigation related to customs, with the peak rate having come down to about 7.5%. The litigation related to central excise, which peaked in the mid 90s, has also drastically come down, with the litigation restricted mainly to interpretation of exemption Notifications, valuation, etc. In the late 90s, there was a lot of litigation on classification issues in central excise, as one would recall but, there is hardly any litigation on classification related issues now.

Well... what's the position as on date?...if one goes by the broad statistics related to cases filed in the CESTAT benches, one would feel that, about 70% to 75% of the cases filed with the CESTAT benches relate

to service tax, with a significant portion of the balance cases relating to central excise, with a negligible quantum of cases being filed in respect of customs related disputes.

That service tax has generated the maximum litigation would seem a bit surprising, given the fact that, despite that service tax was introduced in 1994 (one should heartily thank Dr Manmohan Singh for his ability and wisdom in introducing tax on services for the first time), the potential of this tax was discovered by none other than our beloved Mr P Chidambaram just about 8 years ago. I still remember the 2004 Budget as the giant step towards bringing a lot of services into the tax net. Hence, for all practical purposes, we should consider service tax as an 8 or 9 year old law, when we talk of litigation related issues.

If we had a well-defined law in the first place, that was rightly interpreted by the Revenue, we would not have this quantum of litigation, especially, considering the fact that the Department is the biggest litigant. It is perhaps, only in the service tax law that, different Commissionerates take different stands, on the same subject matter, raising questions on the role of the CBEC.

Be that as it may.... TIOL readers would need to keep in mind that, this quantum of litigation in service tax has arisen, despite having a 'positive service tax law' that we have now. Now, we are scrapping this law which is yet to settle down, and going in for a brand new law, based on an all pervasive definition, which seems to cover all activities except for a handful of services included under the negative list.

I cannot buy the theory that, with this simple definition of "service", the litigation would come down. My strong view is that, the current quantum of litigation would go up by many times over... and the Department would continue to be the biggest litigant. The reasons are not far to seek.

The most unfortunate fact about service tax law is that, this continues to be implemented largely by the folks from the Central Excise Department. The issue is that, most officers of the Central Excise Department, who are veterans in so far understanding of manufacturing and the related physical activities is concerned, have not quite understood the concept of what constitutes a 'service', especially given the fact that, service is a non-physical and non-measurable activity. The ignorance about the concept of service and intellectual property, in the Department, is so high that a high ranking officer, who has spent about 30 years in central excise, asked me as to how a CD containing a packaged software could cost as high as Rs 30 lakhs? He never understood that it was the intellectual property in the form of software that costs Rs 30 lakhs and not the physical medium in which it is encrypted...

Many officers in the service tax department say, in private, that a posting in the service tax department is a 'punishment posting'. The rather low motivation level among the officers of the service tax department, as contrasted to their counterparts in the central excise/customs departments, is for everybody to see. More than anything else, a lack of understanding of what constitutes a 'service' is a contributing factor, perhaps. This being the case, even under the new law with a specific list of 120 odd services... I am not expecting that, things would get any better under the new law, which is an abstract law, to say the least, unless and until there is a paradigm shift in the level of understanding of the departmental officers.

For the new service tax law to work.... it is absolutely essential then, that officers of the service tax department are well trained so that, they are able to handle the transition better. In my view, the success of any law would depend on how it is implemented at the ground level and this is applicable to the new service tax, more than any other law. One hopes that the Government gets its act faster and gets its officers well trained, to face the challenges that the new service tax would throw.

Now.... if the experience of the past few years is any indication... one should see a significant increase in service tax related litigation under the new law, with the ever prevailing need for increase in tax revenues. Will the current trend of service tax related adjudication proceedings being reduced to a farce with proposals

contained in the Show Cause Notices getting confirmed in most cases, without any application of mind as to facts or as to law, I would not believe that, things would change under the new law. On the other hand, things could get worse under the new law.

Consider also the fact that, under the new law, not doing an act, tolerating an act, etc. is a 'declared service'. If I frown upon my neighbour and if he tolerates this activity, this is a service, Sir, believe me, under the new law, rendered by my neighbour to me. This cannot even be contested in a court, as this is a 'declared service'. How would the Department handle these activities is a big question.

And... how about the one page common return for service tax and central excise.... If, with a 17 odd page return separate sheets for each of the services, the Department contends that it is not in the know of things and that the assessee has suppressed the facts, while invoking the extended period... what would be the fate of the assessee when he files a simple one page return.... We don't need to know astrology to predict the response from the Department....

Under the current law, the service tax liability is largely determined on the basis of transactions recorded in the books of accounts. Under the new law, however, the service tax liability would also depend on 'activities' that are not captured in the books of accounts (eg. tolerating an act, a situation, not doing an act, etc), resulting in more confusion and, increased litigation is inevitable.

Before concluding ...

I am wondering as to how a show cause notice would look like, under the new service tax law. If I may hazard a guess... it could be no longer than a half a page or a full page... a far cry from the current situation of a typical SCN running to tens of pages. All that the Department is to allege is that, the activity is a service. As simple as that, Sir. It would be for the assessee to prove that, the said activity is not a 'service'....

In a scenario where SCNs would become so small (in size, of course) and also for the fact that the Department does not even have to issue SCNs in repeat cases.... one should expect the quantum of SCNs to be issued under the new service tax, to increase significantly.

For the Department, consultants like me and the hapless assesseees... all of us have un-learn what we have learnt. In my view... it would be unwise handle the new service tax law, based on our experiences with the existing law. The lesser we try to interpret the new law based on our knowledge of the existing law, the better it is.

There is no doubt that the new service tax law would provide significantly increased professional opportunities for indirect tax practitioners... this seems to be the only positive off-shoot of the new law. Our community is ever grateful to Pranabda for this great development.

As far as TIOL is concerned, I would advise its stakeholders to immediately look for more server space, to report cases out of the CESTAT benches.

I may sound highly negative about litigation related issues under the new service tax law..... I would love to be proved wrong.

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