
(2011) 12 AHC CK 0426
In the Allahabad High Court
Case No : Writ Tax No. 1243 of 2010

M/s Glyph International Ltd

APPELLANT

Vs

Union of India and others

RESPONDENT

Date of Decision : 16-12-2011

Acts Referred:

CENVAT (Credit) Rules, 2004 — Rule 2
Constitution of India, 1950 — Article 12, 14, 245, 246(1), 248
Finance (No. 2) Act, 2004 — Section 95
Finance Act, 1994 — Section 33, 35, 64, 65, 65(105)
Finance Act, 2005 — Section 88
Finance Act, 2007 — Section 140
Income Tax Act, 1961 — Section 9(1)
Service Tax Rules, 1994 — Rule 2(1)

Citation : (2012) 1 ADJ 766 : (2012) 247 CTR 427 : (2011) 189 ECR 13

Hon'ble Judges : Sunil Ambwani, J; K.N. Pandey, J

Bench : Division Bench

Final Decision : Dismissed

Judgement

1. We have heard Shri J.K. Mittal and Shri C.K. Rai for the petitioner-company. Shri S.P. Kesarwani, Additional Chief Standing Counsel appears for the State respondents.

2. The petitioner is a Public Limited Company incorporated under the Companies Act, 1956 having its registered office at C-35, Sector-62, Noida, UP. It was earlier known as "American Devices India Pvt. Ltd", prior to change of its name w.e.f. 11.9.2009.

3. In Writ Petition No. 1243 of 2010, the petitioner has challenged the constitutional validity of Section 66A of Chapter-V of Finance Act, 1994; the Taxation of Services (Provided from Outside India and Received in India) Rules, 2006 and the Instructions F. No.275/7/2010-CX.8A dated 30.6.2010 as ultra vires to the Finance Act, 1994. The petitioner has also prayed for a writ of mandamus to the respondents declaring that the petitioner is not liable to pay

Service Tax on the commission/fee paid to the company located in USA, for promoting and marketing its services in USA.

4. Brief facts giving rise to this writ petition are, that the petitioner is a 100% export oriented unit working under STPI Scheme and holds Customs Bonded License No.13/CUS/STP/2000-2001 dated 11.9.2000, in bond manufacturing sanction order issued by the Deputy Commissioner, Central Excise Division-II, Noida dated 11.9.2000 for manufacture of software. The petitioner is engaged in the e-publishing services, such as data capturing, data conversion, typesetting, formatting, paging, indexing etc. and exports the same to its customers in USA. In other words, the petitioner is editing and setting the contents of the books, which are received from USA.

5. The petitioner is also registered with the Service Tax Authority in the category of, "On-line information and database access and/or retrieval services" vide Service Tax registration No. AAACA6454HST001 dated 13.11.2006 with the Commissioner, Central Excise, Division-II, Noida.

6. The petitioner entered into an agreement dated 29.9.2006 with M/s Software Services LC (SSLC), a company incorporated in USA for promoting and marketing of its business activities in USA.

7. The Service Tax was introduced in India in the year 1994 under Chapter-V of the Finance Act, 1994. Initially only three services were taxable. Since after 1994 the scope of Service Tax has been expanded and that upto the year 2010 there are 114 taxable services. Sections 64, 65, 66, 68, 69 and 70 of the Finance Act, 1994, relevant for the purpose of this case are summarized as below:

(a) Section 64 of the Act defines the geographical boundary of operation of the Act and specifically provides that the Act will extend to whole of India except State of Jammu & Kashmir. Clause (3) of above Section 64 further provides that the Act shall apply to taxable services so provided. The Central Government has also extended the provisions of the Act to Continental Shelf and Exclusive Economic Zone of India; vide Notification No. 14/2010, dated 27.2.2010.

(b) Section 65 of the Act deals with the definitions and more particularly clause (105) of said section deals with the definitions of taxable services.

(c) Section 66 of the Act is the charging section and provides for levy of service tax at the rate of twelve per cent of the value of taxable services. Further, as per Section 95 of the Finance (No. 2) Act, 2004, which has been made effective from 10.9.2004, in addition to the tax chargeable on such taxable services, there are also provisions of levy of an Education Cess at the rate of two per cent of service tax. Further as per the Section 140 of Finance Act, 2007 w.e.f. 12.05.2007, there is provision of levy of secondary and higher education cess at the rate of 1% of service tax.

(d) Section 68 of the Act requires that every person providing taxable service shall pay service tax at specified rate. However, sub-section (2) of Section 68

requires that in respect of notified taxable services, the service tax, thereon, shall be paid by such person and in such manner as may be prescribed at specified rate and in such case, all the provisions of the Act, shall apply to such person as if he is the person liable for paying the service tax in relation to such service. The respondent no. 1 issued the Notification No. 36/2004-ST, dated 31.12.2004 and inter alia notified that for the purpose of sub-section (2) of Section 68, "any taxable service provided or to be provided from a country other than India and received in India, u/s 66A of the Finance Act, 1994".

(e) Section 69 of the Act requires that every person liable to pay the service tax should get registered.

(f) Section 70 of the Act requires that every person liable to pay the service tax shall file return.

8. Under the Service Tax Instructions issued through Circular F. No. B-11/3/98-TRU, dated 7.10.1998 a clarification has been issued in para 7.3 as follows:

7.3. Service tax is payable on all taxable services rendered in India, whether to an Indian or foreign client. However, services rendered abroad shall not attract service tax levy as service tax extends only to services provided within India.

9. The Service Tax Rules, 1994, which came into force from 16.6.2005, were amended in the year 2002 w.e.f. 16.8.2002 by introducing Sub-clause (iv) in clause (d) of sub-rule (1) of Rule 2 vide Notification dated 1.8.2002, providing that a person, who is a non-resident or is from outside India, does not have any office in India, the person receiving the taxable service in India was made liable to pay service tax. The Service Tax Rules, 1994 were further amended by Notification dated 7.6.2005 substituting sub-clause (iv) in clause (d) of sub-rule (1) of Rule 2 consequent to the insertion of Explanation to Section 65(105) of the Act. The amended sub-clause (d) reads as follows:

(d) "person liable for paying the service tax" means, -....

(iv) in relation to any taxable service provided or to be provided by a person, who has established a business or has a fixed establishment from which the service is provided or to be provided, or has his permanent address or usual place of residence, in a country other than India, and such service provider does not have any office in India, the person who receives such service and has his place of business, fixed establishment, permanent address or, as the case may be, usual place of residence, in India.

10. The Service Tax Rules, 1994 were further amended by Notification No. 10/2006-ST dated 19.4.2006. Sub-clause (iv) in clause (d) of Sub-rule (1) of Rule 2, was substituted consequent to the insertion of Section 66A of the Act. The amended Section 66A clause (d) substituted by notification dated 31.12.2004, and thereafter amended again by notification dated 19.4.2006, of which the constitutional validity is under challenge in the writ petition, reads as follows:

(d) "person liable for payment the service tax" means,

(iv) in relation to any taxable service provided or to be provided by any person from a country other than India and received by any person in India u/s 66A of the Act, the recipient of such service.

11. The Finance Act, 1994 was amended on 13.5.2005 by clause (a) of Section 88 of the Finance Act, 2005 adding Explanation to clause (105) of Section 65 w.e.f. 16.6.2005. The explanation reads as follows:

Explanation-For the removal of doubts, it is hereby declared that where any service provided or to be provided by a person, who has established a business or has a fixed establishment from which the service is provided or to be provided, or has his permanent address or usual place of residence, in a country other than India and such service is received or to be received by a person who has his place of business, fixed establishment, permanent address or, as the case may be, usual place of residence, in India, such service shall be deemed to be taxable service for the purposes of this clause;

12. The Ministry of Finance, Government of India issued a Notification No. 25/2005-ST dated 7.6.2005 and granted exemptions for any taxable service provided to an individual by a service provider, where the said taxable services are received and consumed outside India, not in the furtherance of commerce or for any business purpose.

13. With a view to replace the Explanation u/s 65(105) of the Finance Act, 1994 with a substantive provision of law by Finance Act, 2006 w.e.f. 18.4.2006, Section 66A was inserted, which reads as follows:

66A. Charge of service tax on services received from outside India:

(1) Where any service specified in clause (105) of section 65 is,

(a) provided or to be provided by a person who has established a business or has a fixed establishment from which the service is provided or to be provided or has his permanent address or usual place of residence, in a country other than India, and

(b) received by a person (hereinafter referred to as the recipient) who has his place of business, fixed establishment, permanent address or usual place of residence, in India, such service shall, for the purposes of this section, be taxable service, and such taxable service shall be treated as if the recipient had himself provided the service in India, and accordingly all the provisions of this Chapter shall apply:

Provided that where the recipient of the service is an individual and such service received by him is otherwise than for the purpose of use in any business or commerce, the provisions of this sub-section shall not apply:

Provided further that where the provider of the service has his business

establishment both in that country and elsewhere, the country, where the establishment of the provider of service directly concerned with the provision of service is located, shall be treated as the country from which the service is provided or to be provided.

(2) Where a person is carrying on a business through a permanent establishment in India and through another permanent establishment in a country other than India, such permanent establishments shall be treated as separate persons for the purposes of this section.

Explanation 1.- A person carrying on a business through a branch or agency in any country shall be treated as having a business establishment in that country.

Explanation 2.-Usual place of residence, in relation to a body corporate, means the place where it is incorporated or otherwise legally constituted.

14. The Ministry of Finance, Government of India, introduced the Taxation of Service (Provided from outside India and Received in India) Rules, 2006 w.e.f. 19.4.2006 under the newly inserted Section 66A. For the purpose of this case it is useful to reproduce the Rules:

Taxation of Services (Provided From Outside India and Received in India) Rules, 2006

(Notification No. - 11/2006-ST (F. No. B1/4/2006-TRU) dated 19.4.2006 as amended)

In exercise of the powers conferred by sections 93 and 94, read with section 66A of the Finance Act, 1994 (32 of 1994), the Central Government hereby makes the following rules, namely:

1. Short title and commencement

(1) These rules may be called the Taxation of Services (Provided from outside India and Received in India) Rules, 2006.

(2) They shall come into force on the date of their publication in the Official Gazette.

2. Definitions.-

In these rules, unless the context otherwise requires-

(a) "Act" means the Finance Act, 1994 (32 of 1994);

(b) "input" shall have the meaning assigned to it in clause (k) of rule 2 of the CENVAT Credit Rules, 2004;

(c) "input service" shall have the meaning assigned to it in clause (l) of rule 2 of the CENVAT Credit Rules, 2004;

(d) "output service" shall have the meaning assigned to it in clause (p) of rule 2

of the CENVAT Credit Rules, 2004;

(e) "India" includes the installations, structures and vessels located in the continental shelf of India and the exclusive economic zone of India, for the purposes of prospecting or extraction or production of mineral oil and natural gas and supply thereof.

(f) words and expressions used in these rules and not defined, but defined in the Act shall have the meanings respectively assigned to them in the Act.

3. Taxable services provided from outside India and received in India.-

Subject to section 66A of the Act, the taxable services provided from outside India and received in India shall, in relation to taxable services-

(i) specified in sub-clauses (d), (m), (p), (q), (v), (zzq), (zzza), (zzzb), (zzzc), (zzzh), (zzzr), (zzzy), (zzzz), (zzzza), and (zzzzm) of clause (105) of section 65 of the Act, be such services as are provided or to be provided in relation to an immovable property situated in India;

(ii) specified in sub-clauses (a), (f), (h), (i), (j), (l), (n), (o), (w), (x), (y), (z), (zb), (zc), (zi), (zj), (zn), (zo), (zq), (zr), (zt), (zu), (zv), (zw), (zza), (zzc), (zzd), (zzf), (zzg), (zzh), (zzi), (zzl), (zzm), (zzn), (zzo), (zzp), (zzs), (zzt), (zzv), (zzw), (zzx), (zzy), (zzzd), (zzze), (zzzf), (zzzp), (zzzzg), (zzzzh), (zzzzi), (zzzzk), and (zzzzl) of clause (105) of section 65 of the Act, be such services as are performed in India:

Provided that where such taxable service is partly performed in India, it shall be treated as performed in India and the value of such taxable service shall be determined u/s 67 of the Act and the rules made thereunder;

Provided further that where the taxable services referred to in sub-clauses (zzg), (zzh) and (zzi) of clause (105) of section 65 of the Act, are provided in relation to any goods or material or any immovable property, as the case may be, situated in India at the time of provision of service, through internet or an electronic network including a computer network or any other means, then such taxable service, whether or not performed in India, shall be treated as the taxable service performed in India;

(iii) specified in clause (105) of section 65 of the Act, but excluding-

(a) sub-clauses (zzzo) and (zzzv);

(b) those specified in clause (i) of this rule except when the provision of taxable services specified in clauses (d), (zzzc), (zzzr) and (zzzzm) does not relate to immovable property; and

(c) those specified in clause (ii) of this rule, be such services as are received by a recipient located in India for use in relation to business or commerce.

Provided that where the taxable service referred to in sub-clause (zzzzj) of

clause (105) of section 65 of the Act is received by a recipient located in India, then such taxable service shall be treated as taxable service provided from outside India and received in India subject to the condition that the tangible goods supplied for use are located in India during the period of use of such tangible goods by such recipient.

4. Registration and payment of service tax.-

The recipient of taxable services provided from outside India and received in India shall make an application for registration and for this purpose, the provisions of section 69 of the Act and the rules made thereunder shall apply.

5. Taxable services not to be treated as output services.-

The taxable services provided from outside India and received in India shall not be treated as output services for the purpose of availing credit of duty of excise paid on any input or service tax paid on any input services under CENVAT Credit Rules, 2004.

15. The "Business Auxiliary Services" is the new service introduced by amendment of the Finance Act, 2003 w.e.f. 1.7.2003. It covers any service in relation to promotion or marketing or sale of goods including the services provided as a commission agent.

16. The petitioner received a letter dated 18.9.2009 from the office of Commissioner, Central Excise Division-II, Noida with a audit programme for conducting the audit of the records of the petitioner from October 2009. The audit was conducted between 10.10.2009 to 13.10.2009 for the years 2006-07, 2007-08 and 2008 09.

17. The Superintendent, Central Excise, Range-14, Division-II, Noida issued a letter to the petitioner on 18.6.2010 which was received on 5.8.2010, stating that there is non-compliance of the audit objection for the period from April 2008 to March 2009. The letter required the petitioner to send a compliance report by 25.6.2010. A summary of major audit objections from the working paper of the department was also sent along with the letter with directions for necessary action for recovery of government dues. In effect the Superintendent, Central Excise, Range-14, Noida demanded service tax for the services availed by the petitioner from USA based company for promoting their business in USA as per agreement of 19.9.2006 by demanding service tax of Rs. 1, 35, 38, 514/-with interest of Rs. 29, 75, 108/-. The service tax of Rs. 74, 821/-with interest of Rs. 25, 128/-was also demanded on the AMC charges paid to foreign company for upgrading software and also on-line support services. Besides that service charge of Rs. 31, 147/-with interest of Rs. 6,074/-was demanded alleging professional fee paid to the foreign company.

18. In Writ Petition No. 1244 of 2010 the petitioner has prayed for quashing the letter issued by the Commissioner, Central Excise, Customs and Service Tax, Noida dated 18.6.2010 declaring it without any jurisdiction and against the

provisions of law, arbitrary and against the principles of natural justice.

19. The petitioner has raised the issue of the constitutional validity of Section 66A of Chapter-V of the Finance Act, 1994 and the Taxation of Services (Provided From Outside India and Received in India) Rules, 2006 (in short the Rules), as well as the instructions dated 30.6.2010.

20. It is submitted by Shri J.K. Mittal appearing for the petitioner that Section 64 of the Finance Act, 1994 specifies that the provisions of service tax are applicable to the whole of India except State of Jammu and Kashmir. The provisions of the Act thus define geographical boundary of operation of the Act. Any act of receiving or rendering of service outside the territory of India is not amenable to the Finance Act, 1994. He relies upon judgments in Haridas Exports Vs. All India Float Glass Mfrs. Association and Others, in which the Supreme Court applied the "effects doctrine". It was held that Section 2(o) read with Section 2(u) and Section 37 gives jurisdiction to the MRTP Commission to pass appropriate orders qua Restrictive Trade Practice in India. The MRTP Commission, in such a case, may not be able to stop import but there can be an order imposing post import restrictions such as, for example, not to sell imported goods in India in such a manner which will be regarded as a restrictive trade practice. The use of the words "shall be deemed to be an agreement within the meaning of this section..." in Explanation-I to Section 35 and the time-frame for registration clearly indicates that Section 33 and Section 35 apply only to Indian agreements or agreements in India. The Explanation-I was incorporated to enlarge the ambit and give extra territorial jurisdiction in relation to those agreements which relate to performance of services in India, and any party to that agreement carries on business in India. The Supreme Court set aside the order passed by MRTP Commission against the Indonesian exporters.

21. Shri Mittal submits that Section 66A and the Rules of 2006 create another taxable event/incidence of tax from services provided to services received in India, which is against the legislative scheme. It is an artificial event sought to be taxed as many taxable services can never be received in India. The impugned provisions/Rules of 2006 are thus arbitrary, impractical and ambiguous.

22. Shri Mittal submits that Entry 92-C of the Union List to levy "Taxes on Service" inserted by Ninety Fifth Amendment Bill, 2003 (called as 88th Amendment Act, 2003) to the Constitution of India, stated in the objects and reasons that the tax on services is levied in view of significant contribution of the service sector in GDP. The Government always intended to levy tax on the services, which are part of GDP. The services, which are rendered outside India, are not part of GDP, and thus the provision to levy of Service Tax on the services rendered outside India are unconstitutional.

23. Shri Mittal submits that Ministry of Finance, Government of India, in the Circular dated 8.10.2001 has clarified that the service tax leviable extends to whole of India except Jammu and Kashmir, and the term "India" includes its

territorial waters. By Notification dated 27.2.2010 the provisions of Finance Act, 1994 have been extended to Continental Shelf and Exclusive Economic Zones of India as well as installations, structures and vessels within the Continental Shelf and EEZ, that too only for the services specified in the notification. The provisions of the Act, therefore, cannot be applied to the territories beyond the territorial jurisdiction of India, and hence no Service Tax can be levied on the services provided outside India by foreign company irrespective of the fact that the company in India takes the services.

24. Shri Mittal submits that the Ministry of Finance, Government of India has issued clarifications from time to time that the services outside the India do not attract Service Tax. The instructions dated 7.10.1998, "Frequently Asked Questions", issued in October 2003 clearly provided that services outside India do not attract service tax. The instructions dated 16.11.2007 issued by Ministry of Finance also accepts that the incidence of Service Tax is attracted with reference to the place where the service is provided.

25. Shri Mittal submits that the Directorate General of Foreign Trade (DGFT) in its Circular dated 11.4.2008 has clarified that the Service Tax is leviable only on the taxable service provided in India. He submits that unlike the Income Tax Act, 1961, there is no double taxation treaty in Service Tax and therefore, if services rendered by a foreign national in the foreign country is taxed in the hands of citizen of India, it will lead to hardships as the service will be taxed in the country where it was rendered, as well as in India. It will lead to multiple tax of more than one country on the same activity. Shri Mittal has placed reliance upon All India Federation of Tax Practitioners v. Union of India 2007 (7) S.R.T. 625 (S.C.) in which it was held as follows:

5. In late seventies, Government of India initiated an exercise to explore alternative revenue sources due to resource constraints. The primary sources of revenue are direct and indirect taxes. Central excise duty is a tax on the goods produced in India whereas customs duty is the tax on imports. The word "goods" has to be understood in contradistinction to the word "services". Customs and excise duty constitute two major sources of indirect taxes in India. Both are consumption specific in the sense that they do not constitute a charge on the business but on the client. However, by 1994, Government of India found revenue receipts from customs and excise on the decline due to W.T.O. commitments and due to rationalization of duties on commodities. Therefore, in the year 1994-95, the then Union Finance Minister introduced the new concept of "service tax" by imposing tax on services of telephones, non-life insurance and stock-brokers. That list has increased since then. Knowledge economy has made "services" an important revenue-earner.

6. At this stage, we may refer to the concept of "Value Added Tax" (VAT), which is a general tax that applies, in principle, to all commercial activities involving production of goods and provision of services. VAT is a consumption tax as it is borne by the consumer.

7. In the light of what is stated above, it is clear that Service Tax is a VAT which in turn is destination based consumption tax in the sense that it is on commercial activities and is not a charge on the business but on the consumer and it would, logically, be leviable only on services provided within the country. Service tax is a value added tax.

8. As stated above, service tax is VAT. Just as excise duty is a tax on value addition on goods, service tax is on value addition by rendition of services. Therefore, for our understanding, broadly "services" fall into two categories, namely, property based services and performance based services. Property based services cover service providers such as architects, interior designers, real estate agents, construction services, mandapwalas etc.. Performance based services are services provided by service providers like stock-brokers, practising chartered accountants, practising cost accountants, security agencies, tour operators, event managers, travel agents etc..

20. On the basis of the above discussion, it is clear that service tax is VAT which in turn is both a general tax as well as destination based consumption tax leviable on services provided within the country.

26. Reliance has also been placed by Bimal Chandra Banerjee Vs. State of Madhya Pradesh etc., Agricultural Market Committee v. Shalimar Chemicals Works, 1975 (5) SCC 516 ; H. Gangahanume Gowda Vs. Karnataka Agro Industries Corpn. Ltd., and Ishikawajma-Harima Heavy Industries Ltd. Vs. Director of Income Tax, Mumbai, to support his submissions.

27. Shri S.P. Kesarwani, Additional Chief Standing Counsel appearing for the Central Excise Department submits that in October, 2009 the audit team detected that during the period of April 2007, to March, 2009 the petitioner availed services of one M/s Software Services LC (SSLC), to procure orders and to promote business as per a Master Service Agreement dated 29.9.2006 paying them service charges liable to the Service Tax under the category "Business Auxiliary Service" as service recipient u/s 66A of the Finance Act, 1994. The petitioner as recipient of service in India by a foreign company was liable to pay the Service Tax. A request was made to him by the Superintendent of Central Excise by letter dated 18.6.2010 for compliance of objections. This letter was not a notice u/s 73 of the Act, which is yet to be issued. In the proceedings u/s 73 of the Act the petitioner shall be confronted with all evidences and full opportunity will be given to rebut all the allegation of the notice and to submit such evidence as the petitioner may deem fit. The agreement and transactions shall be fully examined and investigated by the adjudicating authority.

28. Shri Kesarwani submits that prima facie the agreement dated 29.9.2006 reveals the facts evidencing that the petitioner is recipient of taxable service (Business Auxiliary Service) and thus the petitioner is liable to pay service tax. He refers to the agreement more particularly the scope, functions and financial terms of the agreement quoted as below:

2. Scope

2.1 The Companies agree that execution of publishing related services, secured by SSLC from the Clients located in the Territory by offshore facility at Noida or such other facilities owned and/or managed by ADIPL shall be covered by this Agreement.

3. Functions

3.1 Execution of Publishing Services

3.1.1. The Companies agree that under this Agreement, ADIPL shall assume the role of the Principal Contractor and shall be responsible for successful execution of all publishing services related contracts.

3.1.2. The Companies acknowledge that such publishing related services shall be executed by ADIPL from its Offshore facility.

6. Financial Terms

6.1 The Companies agree that in order to compensate for the client relationships SSLC has built up in the Territory and for procuring publishing related service contracts, SSLC shall be entitled to a fixed share of the gross revenue receivable from the clients as Compensation fee on a scale-up/down basis as agreed between the Companies. The Companies further agree that the fixed share of revenue shall undergo modification commensurate with the scale of operations as agreed between the Companies from time to time.

29. Shri Kesarwani submits that the agreement executed in India; the petitioner's business place is at Noida where it is receiving the services of a foreign company and from where it is executing contract with its customers in USA. He refers to paras A, B, C, 1 (7, 8), 2.1, 3.1, 3.2, 3.3.7, 4, 5, 14 of the agreement. The agreement is subject to Indian laws applicable for resolution of any dispute between the company and foreign company; the consideration has to be paid under para-6 in India. The service received by the petitioner from a foreign company is "business auxiliary service", as defined in Section 65(19) in India and is liable to tax u/s 65(105)(zzb) read with Section 66A of the Act. He submits that the reliefs claimed in Writ Tax No. 1244 of 2010, against the letter dated 18.6.2010 directing the petitioner to pay service tax with interest is premature, as the show cause notice u/s 73 of the Act has not been issued so far.

30. Shri Kesarwani submits that as per material which has come in the hands of the department by way of audit report of audit team, the petitioner received taxable service provided by the foreign company (SSLC) in India, and thus being a deemed service provider the company is liable to pay service tax.

31. Shri Kesarwani submits that Section 66A is a valid provision. It does not suffer from the vice of unconstitutionality. The Act is referable to Entry 92-C and 97, of List-I of the Seventh Schedule, and Article 246(1) and 248 of the Constitution of India. He has relied upon Tamil Nadu Kalyana Mandapam am

Assn. Vs. Union of India (UOI) and Others, in which the constitutional validity of Section 65 clause 41 sub clause (p) of the Finance Act, 1994, defining the taxable service was upheld and the judgment of the Supreme Court in All India Federation of Tax Practitioners and Others Vs. Union of India (UOI) and Others, in which the legislative competence of the Parliament to levy Service Tax by way of Finance Act, 1994 and 1998 under Entry 97 of List-I on chartered accountants, cost accountants and architects was upheld. In Association of Leasing and Financial Service Companies Vs. Union of India (UOI) and Others, The Supreme Court upheld the levy of Service Tax under Sections 65(12), 65(72), 65(105) (zm), after upholding the validity of Section 66 of the Finance Act, 1994 on the value of taxable services. The Supreme Court found after deciding the validity of the Act, that the writ petitioner should exhaust the statutory remedies, as there has to be an adjudication under the Act. The Supreme Court directed the competent authority under the Finance Act, 1994 to decide the matter in accordance with the law laid down.

32. The Supreme Court held as far back as in 1981 in R.K. Garg and Others Vs. Union of India (UOI) and Others, that every legislation particularly in economic matters is essentially empiric (one who relies on practical experience) and it is based on experimentation. There may be crudities, inequities and even possibilities of abuse but on that account alone it cannot be struck down as invalid. The Court must therefore adjudge the constitutionality of such legislation by the generality of its provisions. Laws relating to economic activities should be viewed with greater latitude than laws touching civil rights such as freedom of speech, religion etc. In paragraphs 7 and 8 the Supreme Court held as follows:-

7. Now while considering the constitutional validity of a statute said to be violative of Article 14, it is necessary to bear in mind certain well established principles which have been evolved by the courts as rules of guidance in discharge of its constitutional function of judicial review. The first rule is that there is always a presumption in favour of the constitutionality of a statute and the burden is upon him who attacks it to show that there has been a clear transgression of the constitutional principles. This rule is based on the assumption, judicially recognised and accepted, that the legislature understands and correctly appreciates the needs of its own people, its laws are directed to problems made manifest by experience and its discrimination are based on adequate grounds. The presumption of constitutionality is indeed so strong that in order to sustain it, the court may take into consideration matters of common knowledge, matters of common report, the history of the times and may assume every state of facts which can be conceived existing at the time of legislation.

8. Another rule of equal importance is that laws relating to economic activities should be viewed with greater latitude than laws touching civil rights such as freedom of speech, religion etc. It has been said by no less a person than Holmes, J. that the legislature should be allowed some play in the joints, because it has to deal with complex problems which do not admit of solution through any

doctrine or straight jacket formula and this is particularly true in case of legislation dealing with economic matters, where, having regard to the nature of the problems required to be dealt with, greater play in the joints has to be allowed to the legislature. The court should feel more inclined to give judicial deference to legislature judgment in the field of economic regulation than in other areas where fundamental human rights are involved. Nowhere has this admonition been more felicitously expressed than in *Morey v. Dond* 354 US 457 where Frankfurter, J. said in his inimitable style:

In the utilities, tax and economic regulation cases, there are good reasons for judicial self-restraint if not judicial difference to legislative judgment. The legislature after all has the affirmative responsibility. The courts have only the power to destroy, not to reconstruct. When these are added to the complexity of economic regulation, the uncertainty, the liability to error, the bewildering conflict of the experts, and the number of times the judges have been overruled by events-self-limitation can be seen to be the path to judicial wisdom and institutional prestige and stability.

The court must always remember that "legislation is directed to practical problems, that the economic mechanism is highly sensitive and complex, that many problems are singular and contingent, that laws are not abstract propositions and do not relate to abstract units and are not to be measured by abstract symmetry" that exact wisdom and nice adoption of remedy are not always possible and that "judgment is largely a prophecy based on meagre and un-interpreted experience". Every legislation particularly in economic matters is essentially empiric and it is based on experimentation or what one may call trial and error method and therefore it cannot provide for all possible situations or anticipate all possible abuses. There, may be crudities and inequities in complicated experimental economic legislation but on that account alone it cannot be struck down as invalid. The courts cannot, as pointed out by the United States Supreme Court in *Secretary of Agriculture v. Central Reig Refining Company* 94 Lawyers Edition 381 be converted into tribunals for relief from such crudities and inequities. There may even be possibilities of abuse, but that too cannot of itself be a ground for invalidating the legislation, because it is not possible for any legislature to anticipate as if by some divine prescience, distortions and abuses of its legislation which may be made by those subject to its provisions and to provide against such distortions and abuses. Indeed, howsoever great may be the care bestowed on its framing, it is difficult to conceive of a legislation which is not capable of being abused by perverted human ingenuity. The Court must therefore adjudge the constitutionality of such legislation by the generality of its provisions and not by its crudities or inequities or by the possibilities of abuse of any of its provisions. If any crudities, inequities or possibilities of abuse come to light, the legislature can always step in and enact suitable amendatory legislation. That is the essence of pragmatic approach which must guide and inspire the legislature in dealing with complex economic issues.

33. In this case the petitioners have basically challenged the validity of Section 66A of the Act on its extra territorial operation. It is alleged that the amendment seeks to levy service tax on the taxable event outside India. It is submitted by the petitioner that any act of receiving or rendering of service outside the territory of India is not amenable to the Finance Act, 1994, with reliance placed on Haridas Exports (supra). The impugned provisions/rules, it is submitted, create another taxable event namely from services provided to services received in India, which is against the scheme of legislation. It has been challenged as artificial, as taxable services can never be received in India. Since no service tax can be levied on the services provided outside India by a foreign company irrespective of the fact that the petitioner has taken the subject services, the extra territorial operation of the act requires to be struck down. It is submitted that the Ministry of Finance, Government of India by its letter dated June 27, 2008 had stated while referring the Board's letter dated 19.4.2006 clarifying admissibility of CENVAT credit of the Service Tax paid u/s 66A on the taxable services provided from outside India, that since the recipient of the service is required to pay the Service Tax u/s 66A, though the service is actually provided not by the recipient but by a person located in a country other than India, such taxable services, not being actually provided by the person liable to pay service tax, are not treated as "output services" for the purpose of CENVAT Credit Rules, 2004; however, service tax paid u/s 66A is available as "input credit" under CENVAT Credit Rules, 2004. Again a clarification was issued on July 16, 2009 that the taxable service u/s 66A in case service is provided from abroad and received in India, such taxable service shall be treated as if the recipient had himself provided the service in India.

34. It was clarified in the letter dated July 16, 2009 issued by the Joint Secretary (TRU-II), Tax Research Unit, Department of Revenue, Ministry of Finance, Government of India, that Section 66A is not a charging section by itself. In fact, it only creates a legal fiction to deem import of service, as provision of service within India, so that the provisions of Chapter-V of the Finance Act, 1994 can be applied to. The charging section remains Section 66, even for the service imported. In other words, the tax collected from the recipient in terms of section 66A, is also tax chargeable u/s 66 of the Finance Act, 1994 and thus there is no mistake in the relevant provision of the CENVAT Credit Rules, 2004 and that credit of tax paid on imported services should be allowed, if they are in the nature of input services.

35. A matter on the demand of service tax under business auxiliary service on the services of overseas commission agents came up for consideration in Commissioner of Central Excise, Ludhiana vs. Bhandari Hosiery Exports Ltd. 2010 (18) S.T.R. 713 (P&H). In this case the assesseees were engaged in the manufacture of hosiery goods and were involved in their export. They availed services of individual overseas commission agents as auxiliary services. A show case notice was issued. It was stated that the assessee was recipient of service of commission agent who is residing outside India. The Adjudicating Authority

confirmed the demand. In appeal the Commissioner (Appeals) set aside the demand to the extent, it was beyond the period of limitation. The Tribunal upheld the order on the premise that Section 66A of the Finance Act, 2006 was enforced with effect from 18.4.2006, which covered the services rendered outside India for imposition of service tax. The Punjab & Haryana High Court found that the Bombay High Court in *Indian National Shipowners Association v. Union of India* 2009 (13) S.T.R. 235 (Bom) following the judgment of the Supreme Court in *Laghu Udyog Bharati v. Union of India* 2006 (2) S.T.R. 276 (SC) upheld the imposition, after the revenue acquired legal authority to levy Service Tax by amendment of the Act on 18.4.2006. Accordingly such a person becomes liable to payment of Service Tax when he received service outside India from a person who is non-resident or is from outside India after 18.4.2006. The Delhi High Court in *Unitech Ltd v. Commissioner of Service Tax, Delhi* 2009 (15) S.T.R. 385 (Del) followed the judgment of Bombay High Court.

36. The constitutional validity on the competence of the Parliament to levy Service Tax has been upheld by the Supreme Court in *Mandampam Association* (supra) decided in the year 2004; *All India Federation of Tax Practitioners* (supra) decided in the year 2007; and the *Association of Leasing & Financial Service Companies* (supra) decided in the year 2010. We are concerned here with the objection to the legislative powers of the Parliament on its extra territorial operations, namely the change in respect of taxable events/incident of the Service Tax, on services provided outside India. The challenge to the constitutionality of the Act is its extra territorial operation in levying the Service Tax on the services provided outside India by a foreign company irrespective of the fact that the petitioner company has taken the said services and has received the benefit of such services.

37. Part XI of the Constitution of India in, Chapter-1-Legislative Relations, provides for distribution of legislative powers. Art. 245 provides for the extent of laws made by Parliament and by legislatures of States subject to the provisions of the Constitution. The Parliament makes laws for the whole or any part of the territory of India, and the legislature of a State may make laws for the whole or any part of State. Clause 2 of Art. 245 provides that no law made by Parliament shall be deemed to be invalid on the ground that it would have extra territorial operation.

38. In *Shrikant Bhalchandra Karulkar and Others Vs. State of Gujarat and Another*, the Supreme Court held that no doubt in view of the provisions of Art. 245 and 246 of the Constitution of India the State legislature has no legislative competence to make laws having extra territorial operation, but so long as law made by State legislature is applicable to the persons residing within its territory and to all things and acts within its territory, it cannot be considered extra-territorial. The doctrine of "territorial nexus" as evolved by the Supreme Court is well established. If there is a territorial nexus between the persons/ property subject matter of the act in the State seeking to comply with the provisions of

the Act, then statute cannot be considered as having extra-territorial operation. In para 7 it is held that the sufficiency of the territorial connection involves consideration of two elements. The connection must be real and not illusory, and the law sought to be imposed under the Act must be relevant to that connection. Same view was taken in the State of Bihar and Ors. v. Shankar Wire Products Industries and Ors., (1995) Supp 4 SCC 646 . The Bihar Weight and Measures (Enforcement) Act, 1959 insisted on verifying and stamping the said weights on demand of fees. These weights were manufactured in Bihar but were meant for sale and delivery in other States. The Supreme Court held that the verification and stamping is on the weights manufactured in the State; it is irrelevant, where the weights are sold, in the State or outside the State. The provisions of stamping have been enacted to protect the interests of the buyers and consumers. It is not unlikely that part of weights may travel to the internal market in the State or after their sale and delivery in other States. In the interests of consumers and keeping in view the object of the legislation, the weights should be verified and stamped at the very inception at the place, where they are manufactured. The provisions of the State Legislature in verifying and stamping the weights cannot, therefore, be said to be beyond its territorial legislative competence.

39. In GVK Inds. Ltd. and Another Vs. The Income Tax Officer and Another, the Supreme Court was not directly concerned with the issue, however, at the instance of the Attorney General, it considered the question to re-examine the rigidity of the view expressed in Electronics Corporation of India Limited Vs. Commissioner of Income Tax and Another, in which it was held that the Parliament's power to legislate, incorporate only competence to enact laws with respect to aspects or causes, that occur, arise or exist, or may be expected to do so, solely within India. The Supreme Court considering the arguments of the Attorney General that the Parliament has inherent power to legislate for any territory including territories, beyond India and that no Court in India may question or invalidate such laws on the ground that they have extra-territorial laws, which in other words views that Parliament may enact legislation even to extra-territorial expects or cause that have no impact, effect in or consequence for India. On considering the scope of Art. 245, the principles of constitutional interpretation, analysis of constitutional topological space and the cases decided by the Privy Council, Australian High Court and the International Law on the concept of sovereignty, and also taking into account the scientific and technological development, which have the magnitude of cross-border travel and transactions including the aspects of crime having global criminal and terror networks, the Supreme Court held that the Parliament is constitutionally restricted from enacting legislation with respect to extra-territorial aspects or causes that do not have, nor expected to have any direct or indirect, tangible or intangible impact or the effect or consequence for the territory of India, or any part of India or the interests of the welfare of the well being of or security of inhabitants of India and Indians. The Supreme Court held in para 124 and 126 as

follows:

124. We now turn to answering the two questions that we set

out with:

(1) Is the Parliament constitutionally restricted from enacting legislation with respect to extra-territorial aspects or causes that do not have, nor expected to have any, direct or indirect, tangible or intangible impact (s) on or effect (s) in or consequences for: (a) the territory of India, or any part of India; or (b) the interests of, welfare of, wellbeing of, or security of inhabitants of India, and Indians?

The answer to the above would be yes. However, the Parliament may exercise its legislative powers with respect to extra-territorial aspects or causes, -events, things, phenomena (howsoever commonplace they may be), resources, actions or transactions, and the like -, that occur, arise or exist or may be expected to do so, naturally or on account of some human agency, in the social, political, economic, cultural, biological, environmental or physical spheres outside the territory of India, and seek to control, modulate, mitigate or transform the effects of such extra-territorial aspects or causes, or in appropriate cases, eliminate or engender such extra-territorial aspects or causes, only when such extra-territorial aspects or causes have, or are expected to have, some impact on, or effect in, or consequences for: (a) the territory of India, or any part of India; or (b) the interests of, welfare of, wellbeing of, or security of inhabitants of India, and Indians.

125. It is important for us to state and hold here that the powers of legislation of the Parliament with regard to all aspects or causes that are within the purview of its competence, including with respect to extra-territorial aspects or causes as delineated above, and as specified by the Constitution, or implied by its essential role in the constitutional scheme, ought not to be subjected to some a-priori quantitative tests, such as sufficiency or significance; or in any other manner requiring a pre-determined degree of strength. All that would be required would be that the connection to India be real or expected to be real, and not illusory or fanciful.

126. Whether a particular law enacted by Parliament does show such a real connection, or expected real connection, between the extra-territorial aspect or cause and something in India or related to India and Indians, in terms of impact, effect or consequence, would be a mixed matter of facts and of law. Obviously, where the Parliament itself posits a degree of such relationship, beyond the constitutional requirement that it be real and not fanciful, then the courts would have to enforce such a requirement in the operation of the law as a matter of that law itself, and not of the Constitution.

127. Does the Parliament have the powers to legislate "for" any territory, other than the territory of India or any part of it?

The answer to the above would be no. It is obvious that Parliament is empowered to make laws with respect to aspects or causes that occur, arise or exist, or may be expected to do so, within the territory of India, and also with respect to extra-territorial aspects or causes that have an impact on or nexus with India as explained above in the answer to Question 1 above. Such laws would fall within the meaning, purport and ambit of the grant of powers to Parliament to make laws "for the whole or any part of the territory of India", and they may not be invalidated on the ground that they may require extra-territorial operation. Any laws enacted by Parliament with respect to extra-territorial aspects or causes that have no impact on or nexus with India would be ultra-vires, as answered in response to Question 1 above, and would be laws made "for" a foreign territory.

40. The Supreme Court also held in *G.V.K. Industries Ltd.* case, that Parliament does not have power to legislate for any territory other than territory of India or part of it and such laws would be ultra vires. It follows, therefore, that the Parliament is empowered to make laws with respect to aspects or cause that occur, arise or exist or may be expected to do so within the territory of India, and also with respect to extra-territorial expects or cause that have an impact on or nexus with India.

41. The charge of the Service Tax to be levied u/s 66A with the enactment of the Finance Act, 2006, is on the services received from outside India. It is not denied that the petitioner company has a fixed business establishment in India. The services by the foreign company, however, it is stated, are not received by the petitioner in India, and is in fact being rendered outside India for promotion of its business. The petitioner is specialised in providing customized solutions to publishing industry which includes publishing related services, composition, art and media services. The SSLC is a Corporation having its presence in Florida, USA and is promoting such services in USA under which SSLC provides front end support to USA based clients. Both the companies have a shared working relationship, under which SSLC has to promote publishing related services in USA to be executed by the petitioner-company in India. By the "Master Services Agreement", dated 29.9.2006 the company decided to realign the business responsibilities and redefine roles and reach of the agreement. The offshore facility, in the definition clause of the agreement, means and includes such facility as owned/maintained by the petitioner for carrying out the publishing related services presently located at Noida and/or such other places, where ADIPL shall set up similar facilities. The publishing related services are defined in the agreement to include services with respect to electronic publishing including but not restricted to indexing, paging, graphics & designing, artwork, drawing & redrawing, conversion, translation, type setting, copy editing, multimedia solutions etc. under the agreement purporting to realign the business responsibilities and redefining the roles and reach, it was decided that the scope of the agreement would be to execute publishing related services, secured by SSLC from the clients located in the territory (in U.S.) by offshore facility at

Noida. The functions under the agreement include the petitioner to assume the role of the principal contractor for successful execution of all publishing services related contracts. All the publishing related services are to be executed by the petitioner from India. The financial terms provide that the petitioner company shall be entitled to a fixed share of gross revenue receivable from the clients as compensation fee on a scale-up/down basis. The fixed share of revenue shall undergo modification commensurate with the scale of operations as agreed between the companies from time to time. Prima facie, on these terms, we find that the taxable services provided from outside India, are received and can be taxed in India u/s 66A(1)(b) of the Act.

42. So far as the argument of double taxation is concerned, it was held by the Supreme Court in *Ishikawajima-Harima Heavy Industries Ltd vs. Director of Income Tax, Mumbai* (supra) that payment by a resident to a non-resident by way of fees for technical services must have sufficient territorial nexus with India so as to furnish a basis for imposition of tax. The Supreme Court laid down a test of double taxation namely that the services, which are source of income that is sought to be taxed, has to be rendered in India as well as utilised in India. Where both these conditions are not satisfied, the income is excluded from the ambit of taxation in India. It was further held that only such part of income as is attributable to operations carried out in India, can be taxed in India. For profits to be attributable directly or indirectly, permanent establishment must be involved in activity giving rise to profits. The Court while interpreting Section 9(1) (vii) of the Income Tax Act held that it is necessary that the services not only be utilised within India, but also rendered in India or have such a live link with India that the entire income from fees as envisaged in Article 12 of the Double Taxation Avoidance Agreement (Between India and Japan) becomes taxable in India. In the facts of the case the Court held that there was nothing to show that the income derived by a non-recipient company irrespective of were rendered was utilised in India and since the entire services were rendered outside India have nothing to do with the permanent establishment, could not be held to be attributable to the permanent establishment and therefore not taxable in India. The case was decided on its own facts interpreting the Double Taxation Avoidance Agreement, and the contracts between the parties.

43. At this stage without there being any adjudication, it is difficult to accept that the SSLC is providing any offshore facility to the petitioner to carry out the business operations under the realigning agreement. The scope of the agreement clearly shows that the SSLC as a foreign company has to procure the business and that the publishing related activities have to be performed by the petitioner company on its offshore facility at Noida or such other facilities owned or managed by the company.

44. At this stage we are unable to appreciate the argument that the terms and conditions of the agreement provide for services to be rendered by the foreign company with which the business under realigned agreement has no concern. We

are also unable to comment and to decide until the adjudication is made, nor it is advisable to decide at this stage that the services rendered by the foreign company for procuring business or such services which are not rendered to the petitioner company either offshore or in India. These matters are left to be considered after a notice is given to the petitioner for adjudication, to which the petitioner will have adequate opportunity to object and to produce all such material as may be necessary.

45. We thus hold that Section 66A as inserted by Finance Act, 2006 vide notification dated 18.4.2006 w.e.f. 1.5.2006 providing charge of service tax on services received from outside India provided, or to be provided by a person, who has established a business or has a fixed establishment from which the services are provided and are received by a person (recipient), who has his place of business, fixed establishment, permanent address or usual place of residence in India to be taxable services and the Taxation of Services (Provided from Outside India) Rules, 2006 made in exercise of powers conferred by Sections 93 and 94 read with Section 66A of the Finance Act, 1994 notified on 19.4.2006 and amended by notification dated 27.2.2010, does not suffer from vice of unconstitutionality, either on the ground of lack of legislative competence, or on the ground of extra territorial operation of laws. So far as the levy of the Service Tax on the services alleged to be received by the petitioner from Software Services LC (SSLC) having its office in USA under the "Master Services Agreement", and for which the letter dated 18.6.2010 has been sent to the petitioner on the basis of an audit report of the audit inspection, since there has been no adjudication under the Act, we direct that the competent authority under the Finance Act, 1994 to decide the matter in accordance with the law laid down.

46. The Writ Petition No. 1243 of 2010 is dismissed and the WritPetition No. 1244 of 2010 is disposed of accordingly.