

STAX levy on financial leasing is legal

Giving a jolt to practice of challenging demand of service tax in High Courts by filing Petitions; Full Bench of SC has ruled that service tax on financial leasing services including equipment leasing and hire-purchase is within the legislative competence of the Parliament.

Dismissing the Appeal of Association of Leasing & Financial Service Companies; Full Bench of Supreme Court vide a Ruling dated 26th October, written by Chief Justice SH Kapadia has ruled that **“the service tax in the present case is neither on the material nor on sale. It is on the activity of financing/funding of equipment/asset within the meaning of the words "financial leasing services" in Section 65(12)(a)(i).**

The appellant(s) had moved the High Court in the writ petition challenging the validity of Section 66 of the Finance Act, 1994 on the value of taxable services referred to in Section 65(105)(zm) read with Section 65(12)(a)(i) without exhausting the statutory remedy. The contracts entered into by the appellant(s) with its customers were not vetted. There has been no adjudication under the Act in most of these cases and, therefore, we hereby direct the competent authority under the Finance Act, 1994 to decide the matter in accordance with the law laid down. Subject to above, for the afore-stated reasons, we hold that the service tax imposed by Section 66 of the Finance Act, 1994 (as amended) on the value of taxable services referred to in Section 65(105)(zm) read with Section 65(12) of the said Act, insofar as it relates to financial leasing services including equipment leasing and hire-purchase is within the legislative competence of the Parliament under Entry 97, List I of the Seventh Schedule to the Constitution.”

Being aggrieved by the inclusion of hire-purchase and leasing services within the service tax net, the appellant herein challenged the amendment of 2001 as ultra vires the legislative competence of the Parliament. By the impugned judgment, the Madras High Court dismissed the writ petition, and hence, the civil appeal was filed in Supreme Court.

SC has commented that with the technological advancement there is a very thin line which divides a "sale" from "service". That, applying the principle of equivalence, there is no difference between production or manufacture of saleable goods and production of marketable/saleable services in the form of an activity undertaken by the service provider for consideration, which correspondingly stands consumed by the service receiver. It is this principle of equivalence which is inbuilt into the concept of service tax under the Finance Act, 1994. That service tax is, therefore, a tax on an activity. That, service tax is a value added tax. The value addition is on account of the activity which provides value addition, for example, an activity undertaken by a chartered accountant or a broker is an activity undertaken by him based on his performance and skill. This is from the point of view of the professional. However, from the point of view of his client, the chartered accountant/broker is his service provider. The value addition comes in on account of the activity undertaken by the professional like tax planning, advising, consultation etc. It gives value addition to the goods manufactured or produced or sold. Thus, service tax is imposed every time service is rendered to the customer/client. This is clear from the

provisions of Section 65(105)(zm) of the Finance Act, 1994 (as amended). Thus, the taxable event is each exercise/ activity undertaken by the service provider and each time service tax gets attracted. The same view is reiterated broadly in the earlier judgment of this Court in *Godfrey Phillips India Ltd. v. State of U.P.* [(2005 (2) SCC 515)] in which a Constitution Bench observed that in the classical sense a tax is composed of two elements : the person, thing or activity on which tax is imposed. Thus, every tax may be levied on an object or on the event of taxation. Service tax is, thus, a tax on activity whereas sales tax is a tax on sale of a thing or goods.

Merely because for valuation purposes inter alia "finance/ interest charges" are taken into account and merely because service tax is imposed on financial services with reference to "hiring/ interest" charges, the impugned tax does not cease to be service tax and nor does it become tax on hire- purchase/ leasing transactions under Article 366(29A) read with Entry 54, List II. Thus, while State Legislature is competent to impose tax on "sale" by legislation relating to Entry 54 of List II of Seventh Schedule, tax on the aspect of the "services", vendor not being relating to any entry in the State List, would be within the legislative competence of the Parliament under Article 248 read with Entry 97 of List I of Seventh Schedule to the Constitution.

SC has on three different occasions upheld the levy of service with reference to Entry 97 of List I in the face of challenges to the competence of the Parliament based on the entries in List II and on all the three occasions held that the levy of service tax falls within Entry 97 of List I.

Many Consultants advise their clients to challenge every demand notice by filing Petition in High Court while 99 per cent petitions are dismissed by High Courts.

The clients pay a high cost of litigation by engaging lawyers who charge up to Rs 5 lakh per appearance. The matter again starts with adjudication of notice by Adjudicating Authority.

With this landmark SC Ruling; the taxpayers need to re-visit their approach instead of wasting their time and resources. They should not forget that the delay in payment of tax also attracts interest at the rate of 13 per cent and penalty under Section 76/78 of Finance Act, 1994 which can be equal to service tax involved. The option of taking litigation to High Court/Supreme Court is always open even after departmental adjudication and decision by CESTAT. Cutting short of litigation is always a better option than lingering of litigation for a taxpayer; though the better option for a lawyer may be reverse approach