

TAX FLASH NEWS

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Service tax is not payable on the portion of TDS borne by recipient

Customs, Excise and Service Tax Appellate Tribunal, Chennai¹ has held that TDS under Income Tax Act, 1961 is a statutory obligation and cannot be treated as consideration for the purpose of service tax under Finance Act, 1994. Thus, service tax is not payable on the gross amount on account of TDS.

Facts of the case

- 'Appellant' is engaged in the manufacturing of motor vehicles and IC engines.
- During the period March 2004 to September 2007, it received consultancy services from service providers not having offices in India. On such services, 'Appellant' has paid service tax under reverse charge mechanism. While paying such service tax, it did not include TDS for determining the taxable value on which service tax is paid.
- Department issued a SCN and subsequently confirmed the demand on the grounds that 'Appellant' is liable to pay service tax even on TDS portion while paying consideration to foreign service providers.

Appellant's Contentions

- As per terms of agreement with the foreign service provider, the consideration payable by the 'Appellant' would be net of all duties and taxes.
- As per section 195 of the Income Tax Act, 1961, 'Appellant' is liable to deduct income tax on such payments. TDS to be borne by 'Appellant' is worked out in terms of section 195A (supra). To illustrate, if agreed consideration is INR 100 and TDS rate is 10% then gross amount worked out for the purpose of TDS is INR 111 and TDS on such gross amount is INR 11. Grossing up of consideration to INR 111 is only for the purpose of income tax and consideration for service tax remains to be INR 100.

- In terms of section 67 of Finance Act, 1994, value for the purpose of service tax is actual amount charged by foreign service provider on which it has discharged appropriate service tax.

Department's Contentions

- In terms of section 67 (supra), value on which service tax is chargeable in case where provision of service is for a consideration in money will be gross amount charged by service provider.
- As the 'Appellant' has grossed up the value along with TDS, TDS amount has to be included in taxable value for discharging service tax liability

Tribunal's Decision

- Section 195A of the Income Tax Act, 1961 states that income shall be increased for the purpose of TDS in cases where tax is to be borne by person in terms of an agreement or other arrangement. Accordingly, 'Appellant' has grossed up TDS for statutory compliance under Income Tax Act.
- TDS amount cannot be treated as 'consideration' for services rendered. In terms of definition of 'consideration' as per Indian Contract Act, 1872, amount paid at will of a person not a party to the agreement does not bear the character of 'consideration'. Thus, amount on which the parties have reached *consensus ad idem* can only be consideration for the services.
- Demand of service tax cannot be sustained on account of *res judicata* in a catena of decisions which has categorically held that on a plain reading of section 67 of the Finance Act, 1994, service tax liability will not arise if assessee has borne the TDS amount.

¹ T.V.S. Motor Company Limited vs. The Commissioner Of Central Excise & Service Tax, Chennai- [2021-VIL-412-CESTAT-CHE-ST]

Our comments

This has been a debatable point and there are contrary judgments on the same. In GST, section 15 states that value of supply shall be transaction value and shall include taxes, duties, cesses, fees and charges levied under any law. Given that the provisions of valuation for the purpose of levy of GST is different from service tax, it would be interesting to see if the *status quo* of the principle of *ratio decidendi* discussed above would also be appreciated under GST.



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