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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

\+ W.P. (C) 5666/2010, CM APPL.8963/2014

M/S ALKARMA ..... Petitioner

Through: Ms. Parul Dureja, Advocate.

versus

UOI & ORS ..... Respondents

Through: None.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE NAJMI WAZIRI

<u>O R D E R</u>

% **08.12.2016**

None present for the respondents.

The issue involved in this petition which seeks multiple reliefs, is whether the show cause notice dated 11.02.2009 calling upon the petitioner why it should not be proceeded against for wrongly availing the benefit under Notification Nos.15/2004-ST dated 10.09.2004, 18/2005-ST dated 7.6.2005 and 1/2006-ST dated 1.3.2006 and Works Contract (Composition Scheme for Payment of Service Tax), Rules, 2007 should not be drawn. The show cause notice recites that the petitioner was availing a self assessment procedure and had not disclosed that it was providing only completion and finishing services in relation to building or civil structures and that it had received materials such as glass and aluminium free of cost from their clients and that value of such materials was not added and disclosed to the service tax authorities while reporting taxable turn over. The petitioner also impugns a Circular dated 4.1.2008, inasmuch as it clarifies that goods free of cost would also be leviable to service tax.

The construction service *per se* was included as a taxable service with the introduction of Section 65 (105) (zzq). In furtherance of the power to issue rules, the respondents issued Notification No.1/2006. In Item no.7 to the explanation to that Notification, the value of goods and materials supplied or provided or used by the service provider is part of the taxable turnover value. The petitioner submits that the impugned Notification - and indeed the show cause notice - proceeded on the erroneous assumption, that inclusion of the value of free materials was a part of the turnover.

The respondents resist the proceeding and rely upon Section 65 (105) (zzq) which explains that construction contract could be of two types, i.e., firstly of a labour contract for construction or contract for construction including material used partly or fully, provided by the service recipient. Service Tax, according to the respondents, is leviable on the gross amount charged by the service provider. Reliance is placed upon *Advertising Club v. Central Board of Excise and Customs*, 2001 (131) ELT 35 (MAD.).

At the time of admission and in subsequent proceedings, this Court had noticed that the issue urged in this petition is connected with the challenge in W.P. (C) 3048/2008 *Era Infra Engineering Ltd. v. UOI* as well as *Y.F.C. Projects Pvt. Ltd. v. UOI* -

W.P.(C)1342/2008 and connected cases (W.P.(C) 859/2008, 4116/2008, 6058/2008 and 6803/2013). All these, however, concerned the levy under Section 65 (105) (zzd), (zzq) and (zzh). Those writ petitions were disposed of on 9.1.2014 *inter alia* in terms of the following directions: -

> *"16. The grievance of the petitioner with regard to assessment and computation cannot be equated with the challenge to the constitutional validity of the impugned provisions. It is open to the petitioner to raise issues of computation before the appropriate Adjudicating Authority/Appellate Authority and demonstrate the extent to which service tax can be imposed on the services that are provided by them. To be clear, it is open to the petitioner to demonstrate the extent of the service element included in the composite contract and to pay service tax only on that component.*
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> *17. The Division Bench in G.D. Builders (supra) has already interpreted the impugned provisions and has taken the view that it is only the service element which is to be taxed under the impugned provisions. We agree with that view. As such, there is no encroachment by Parliament on the exclusive powers of the State Legislature in respect of Entry No.54, List II and, therefore, the said provisions are constitutional. The computation of service tax is, of course, left to the Adjudicating Authority/Appellate Authority.*
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> *18. Insofar as the question of the ready-mix concrete is concerned, it is true that the petitioner manufactures the same and either supplies it to third parties or uses it in its own works. It is not the entire ready-mix concrete which is to be taxed under the provisions of service tax but, only the service element in relation to the use of the ready-mix concrete which would be amenable to service tax. Therefore, in the case of ready-mix concrete also the challenge does not hold good."*

This Court further notices that in *Intercontinental Consultants and*

Technocrats Pvt. Ltd. v. UOI, 2013 (29 STR) Del, had held invalid a similar provision, i.e., Rule 5 (1) of the Service Tax Rules, 2006.

The discussion in *Intercontinental* is as follows: -

> *"18. Section 66 levies service tax at a particular rate on the value of taxable services. Section 67 (1) makes the provisions of the section subject to the provisions of Chapter V, which includes Section 66. This is a clear mandate that the value of taxable services for charging service tax has to be in consonance with Section 66 which levies a tax only on the taxable service and nothing else. There is thus in built mechanism to ensure that only the taxable service shall be evaluated under the provisions of 67. Clause (i) of sub-section (1) of Section 67 provides that the value of the taxable service shall be the gross amount charged by the service provider "for such service". Reading Section 66 and Section 67 (1) (i) together and harmoniously, it seems clear to us that in the valuation of the taxable service, nothing more and nothing less than the consideration paid as quid pro quo for the service can be brought to charge. Sub-section (4) of Section 67 which enables the determination of the value of the taxable service "in such manner as may be prescribed" is expressly made subject to the provisions of sub-section (1). The thread which runs through Sections 66, 67 and Section 94, which empowers the Central Government to make rules for carrying out the provisions of Chapter V of the Act is manifest, in the sense that only the service actually provided by the service provider can be valued and assessed to service tax. We are, therefore, undoubtedly of the opinion that Rule 5 (1) of the Rules runs counter and is repugnant to Sections 66 and 67 of the Act and to that extent it is ultra vires. It purports to tax not what is due from the service provider under the charging Section, but it seeks to extract something more from him by including in the valuation of the taxable service the other expenditure and costs which are incurred by the service provider "in the course of providing taxable service". What is brought to charge under the relevant Sections is only the consideration for the taxable service. By including the expenditure and costs, Rule 5(1) goes*

> *far beyond the charging provisions and cannot be upheld. It is no answer to say that under sub-section (4) of Section 94 of the Act, every rule framed by the Central Government shall be laid before each House of Parliament and that the House has the power to modify the rule. As pointed out by the Supreme Court in Hukam Chand v. Union of India, AIR 1972 SC 2427: -*
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> > *"The fact that the rules framed under the Act have to be laid before each House of Parliament would not confer validity on a rule if it is made not in conformity with Section 40 of the Act."*
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> *Thus Section 94 (4) does not add any greater force to the Rules than what they ordinarily have as species of subordinate legislation."*

Likewise in *Bhayana Builders,* the Larger Bench of the CESTAT after noticing the order in *Intercontinental (supra)* concluded as follows: -

> *"(vi) In* ***Intercontinental Consultants and Technocrats Pvt. Ltd. Vs. Union of India***[1]*, the Delhi High Court was essentially considering a challenge of the validity of Rule 5 of the Service Tax (determination of value) Rules, 2006. This provision was challenged to the extent it includes reimbursement of expenses in the value of taxable services for the purpose of levy of service tax. Apart from the challenge to its constitutionality, the provision was challenged on the ground that it is ultra vires the provisions of Sections 66 and 67 of the Act. The High Court held that section 66 of the Act levies tax only on the taxable services; that this is an inbuilt mechanism to ensure that only the taxable service shall be evaluated under the provisions of Section 67; that on construing the provisions of Sections 66 and 67 (1)(i) together and harmoniously, it is clear that the value of taxable service shall be the gross amount charged by the service provider; and nothing more and nothing less than the consideration paid as a quid pro quo for the service can be brought to charge. The High Court further held that the common thread that runs through Sections 66 and 67*

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[1] 2013 (29 STR) DEL

and 94 (the Rule making power), manifests that only the service actually provided by the service provider can be valued and assessed to tax. The High Court concluded that the provisions of Rule 5(i) of the valuation Rules are repugnant to Sections 66 and 67 of the Act since the provision purport to tax not, what is due from the service provider under the charging section, but seeks to extract something more from him by including in the valuation of the taxable service other expenditure and costs which are incurred by the service provider in the course of providing taxable service.

(vii) In the light of the clear Legislative text, the unambiguous provisions of sections 66 and 67 of the Act and in the light of the judgment in ***Intercontinental Consultants and Technocrats Pvt Ltd.*** *(supra), the conclusion is compelling and inviolable that the value "free supplies" by a construction services recipient, for incorporation in the constructions would not constitute a non-monetary consideration to the service provider nor form part of the gross amount charged for the services provided. Whether the legislature may enact that the value of "free supplies" should be included in the value of the service provided for levy of tax; and within its legislative competence, is an aspect that is speculative for the nonce and outside the purview of either the substantive appeals or the issue referred to us. In this view of the matter it is not necessary to consider the contention on behalf of the assessees that an interpretation that Section 67 of the Act enables or mandates inclusion of the value of goods and materials incorporated into construction services (whether provided by the service provider or as a free supplies by the service recipient) would render the legislative provision unconstitutional, since value of the goods incorporated being sale of goods would be liable to sales tax, an area within the legislative competence of State, the value of goods sold would thus be beyond the legislative competence of Parliament for levy of tax on such sale; consequently could not also constitute the value of taxable services. Ld. Counsel placed reliance on the judgment in* ***M/s Gannon Dunkerley and Co. and Others vs. State of Rajasthan and Others[2]; and State of Andhra***

[2] (1993) 1 SCC 364

Pradesh and Others vs. Larsen & Toubro Limited and Others[3]*, to buttress this contention.*

(viii) Since Section 67 of the Act, as currently structured does not, in our view require inclusion of free supplies in the gross value charged, for computation of the value of taxable services; and as this is the only issue presented (on Section 67 of the Act); we find no justification for a wider analysis of a speculative theatre, of potential conflict."

In view of the above rulings as well as the judgments of this Court in *Era Infra Engineering Ltd. v. UOI*, W.P.(C)3048/2008, decided on 17.10.2016, this writ petition has to succeed. The impugned show cause notice is hereby quashed. The respondents are directed to proceed strictly in accordance with the directions in *Era Infra Engineering Ltd.* and *Y.F.C. Projects Pvt. Ltd. (supra)* and exclude the value of free materials used by the petitioner in its commercial/business activities.

The writ petition is allowed in the above terms. There shall be no order as to costs.

S. RAVINDRA BHAT, J

NAJMI WAZIRI, J

DECEMBER 08, 2016
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[3] (2008) 9 SCC 191