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SC holds that no service tax is payable on reimbursable expenditure or cost incurred by the service provider before 14 May, 2015

Background

Section 67 of the Finance Act, 1994 (the FA, 1994) deals with the valuation of taxable services for the purpose of levy of service tax. Further, the Service Tax (Determination of Value) Rules, 2006 (the Rules) were also issued, to specify inclusion or exclusion of various amounts in the value of taxable services. The assessee had challenged the inclusion of amounts of reimbursable expenditure recovered from the customer in value of taxable services. The Delhi High Court (HC) decided the issue in favour of the assessee and held that service tax was not applicable on the amount of reimbursable expenditure. The tax authorities appealed against this decision in the Supreme Court (SC). In the meanwhile, section 67 of the FA, 1994 was amended to specifically include the amount of reimbursable expenditure in the value of taxable services.

SC's decision[1]

The SC rejected the appeal filed by the tax authorities and observed as under:

- Undoubtedly, rule 5 of the Rules brings within its sweep the expenses which are incurred and reimbursed by the service receiver to the service provider while providing the service. As per these rules, reimbursable expenses also form part of the 'gross amount charged'. Therefore, the core issue in the appeal is whether section 67 of the FA, 1994 permits the subordinate legislation to be enacted in the said manner, as done by Rule 5.
- Section 66 of the FA, 1994 specifically mentions that the service tax will be on the 'value of taxable services'. Thus, service tax is to be determined with reference to the value of services which are actually rendered.
- In section 67 of the FA, 1994, the expression 'such' is important and in deciding the value of taxable services for charging service tax, the authorities had to find out what was the gross amount charged for providing 'such' taxable services.
- Any other amount which was calculated not for providing such taxable service could not form part of valuation as that amount was not for providing such 'taxable service'.
- Accordingly, rule 5 of the Rules went much beyond the mandate of section 67 and the Delhi HC was right in interpreting sections 66 and 67 to hold that the value of taxable service shall be gross amount charged by the service provider 'for such service' and the valuation for service tax could not be anything more or less than the consideration paid *as quid pro quo* for rendering such a service.
- The amendment in section 67 with effect from 14 May, 2015 to include the reimbursable expenditure within the meaning of 'consideration' was a substantial change in the law and had to be prospective in nature.

The Court also held that the value of free supplies of diesel and explosives by the recipient of service would not warrant inclusion in the value of gross amount charged by the service provider for the purposes of payment of service tax and that is not a consideration for rendering the service.

The takeaways

The SC decision comes as a huge relief to the assessees who have been litigating levy of service tax on reimbursable expenditure before 14 May, 2015. The industry may assess the implications of this decision under the GST regime. The GST Act specifically provides for inclusion of incidental expenses charged by the supplier in the value of supply and the Valuation Rules provide for exclusion of expenditure incurred as a pure agent.

[1]Civil Appeal No. 2013 of 2014 (TS-72-SC-2018-ST)

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