S.S. RANA & CO.
ADVOCATES

India: Delhi High Court rules on the issue of payment of service tax by tour operators during the period between July 2012 to July 2017

Brief Background

The Writ Petition was filed by the Indian Association of Tour Operators (hereinafter referred to as the 'Petitioners'), which is the National Body of the tourism industry. Established in 1982, it has over 1600 members covering all segments of the Tourism Industry. In the present instance, the Petitioners seek two things -

1. a declaration by the Delhi High Court that Rule 6A of the Service Tax Rules, 1994 (hereinafter referred to as the 'ST Rules') concerning 'Export of Services' is *ultra vires* the Finance Act, 1994 (hereinafter referred to as the 'Finance Act').
2. Challenges the validity of Section 94 (2) (f) of the Finance Act on the ground that it gives unguided and uncontrolled power to the Central Government to frame rules regarding 'provisions for determining export of taxable services'.

A lot of members of the Petitioners are Indian tour operators who are engaged in the business of arranging tours for foreign tourists visiting India as well as the neighboring countries in the Indian Sub-continent. They enter into contracts with their foreign clients either directly or through foreign tour operators. The Petitioners also state that the foreign tourists/foreign tour operators make the entire payment for the package tour in convertible foreign exchange through bank transfer, or bank draft or credit card payments, etc.

The Petitioners state that prior to insertion of Section 6A of the ST Rules with effect from July 1, 2012, tour operator services provided to foreign tourists were treated as 'Export of Services' and exempted from the levy of service. The invoices further submitted by the Petitioners that were raised after July 1, 2012 reveal that service tax @ 3.09 % is charged on the cost of services provided by the Indian tour operators to foreign tourists.

However, with the introduction of the Goods and Service Tax regime with effect from July 1, 2017, the provisions of the earlier Finance Act became redundant, and thus, the Petitioners are

only concerned with the legal position as it existed prior to July 1, 2017. *Thus, the present Writ Petition is concerned with the question of payment of Service Tax by the Indian tour operators in respect of the services provided by them to foreign tourists during the period between July 1, 2012 and July 1, 2017.*

However, before proceeding into the arguments advanced from both the sides, let us first look into the history and evolution of the Acts and Rules that are *germane* to the present petition.

Position Prior to July 1, 2012

a. Service Tax was introduced for the first time by the Finance Act, with effect from July 1, 1994.
b. The relevant provisions concerning service tax were set out in Chapter V of the Finance Act.
    i. Section 64 (1) stated that Chapter V will be applicable to the whole of India except Jammu and Kashmir
    ii. Section 64 (3) provided that it would apply to 'taxable services provided on or after the commencement this Chapter'.
    iii. Section 65 (105) of the Finance Act defined 'taxable service' to mean 'any service provided or to be provided' to a whole range of persons as mentioned in clauses (1) to (zzzzw)
    iv. Clause (m) of Section 65 (105) of the Finance Act, stated that the provision of service to any person 'by a tour operation in relation to a tour' would be a taxable service.
    v. Section 66 of the Finance Act provided for the 'charge of service tax' at the rate of 12 % of the value of the taxable service referred to in Section 65 (105) (n).
    vi. Section 93 (1) of the Finance Act empowered the Central Government to exempt a taxable service of any specified description.
    vii. The rule making power of the Central Government is provided in Section 94. Section 94 (1) states that the Central Government may make rules for carrying out the provisions of Chapter V of the Finance Act which pertained to service tax.
    viii. Section 94 (2) permits the Central Government to make rules on matters specified therein "without prejudice to the generality of" the power under Section 94 (1).
    ix. Section 94 (2) (f) permits the Central Government to make rules 'for determining export of taxable service'.
c. On the strength of Sections 93 and 94 (2) (f) of the Finance Act, the Central Government issued the Export of Services Rules, 2005 (hereinafter referred to as 'ESR 2005').

i. Rule 3 (1) (ii) ESR 2005 *inter alia* stated that "export of taxable services shall in relation to taxable services specified in sub-clause (n) of clause (105) of Section 65 of the Act, be provision of such services as are performed outside India".
ii. The proviso thereto stated that where such taxable service is partly performed outside India, "it shall be treated as performed outside India."
iii. Rules 3 (2) of ESR 2005 initially stated that the provision of any taxable service specified in Rule 3 (1) shall be treated as export of service when the following conditions are satisfied, viz.:
    1. such service is delivered outside India and used outside India; and
    2. payment for such service provided outside India is received by the service provider in convertible foreign exchange.
iv. The Explanation to the Rule 3 (2) stated: "for the purposes of this rule 'India' includes the installations, structures and vessels in the continental shelf of India and the exclusive economic zone of India."
v. Rule 3 (2) of ESR 2005 underwent changes first in 2007 and then again in 2010. As a result of these amendments, Rule 3 (2) ESR read thus

3 (2) The provision of any taxable service specified in sub-rule (1) shall be treated as export of service when the following conditions are satisfied, namely:

(a) (omitted)

(b) payment for such service is received by the service provider in convertible foreign exchange

vi. The Explanation to Rule 3 (2) too underwent a change and read thus after the 2010 amendment: "For the purposes of this rule 'India' includes the installations, structures and vessels 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 supply thereof."
vii. Rule 4 of the ESR 2005 stated: "Any service, which is taxable under clause (105) of Section 65 of the Act, may be exported without payment of service tax."

d. The resultant position, prior to July 1, 2012, as far as export of tour operator services was that even if a part of the service was performed outside India and the remaining was performed in India, then it would still be treated as having been performed outside India and thereby be construed as an export of service. Such export of tour operator service was not exigible to service tax.

Position after July 1, 2012

a. Significant changes were introduced in Chapter V of the Finance Act with effect from July 1, 2012 by the Finance Act, 2012.

i. Section 65 was omitted and substituted by Section 65 B titled 'Interpretations'.
ii. Section 65 B (51) of the Finance Act, defined the expression 'taxable service' to mean any service on which service tax is leviable under Section 66B. Section 66B is the charging provision.
iii. Section 66 B of the Finance Act, inserted by the Finance Act, 2012, with effect from July 1, 2012, provided that: "there shall be levied a tax at the rate of 12 per cent on the value of all services, other than those services specified in the negative list, provided or agreed to be provided in the taxable territory by one person to another and collected in such manner as may be prescribed."
iv. A plain reading of the charging provision, Section 66 B of the FA, brings out the following facets:
    1. Service tax is leviable on the value of all services "other than those services specified in the negative list." The negative list of services are set out in Section 66D of the Finance Act, inserted again with effect from July 1, 2012. Tour operator services is not part of the negative list.
    2. Such service should be "provided or agreed to be provided" by one person to another and collected in such manner as may be prescribed.
    3. Such service should be provided or agreed to be provided in the "taxable territory". The expression 'taxable territory' has been defined under Section 65B (52) to mean "the territory to which the provisions of this Chapter apply."
v. A collective reading of Section 66 B read with Section 64 (1) and Section 65B (52) makes it plain that service tax is leviable only on services provided or agreed to be provided in the 'taxable territory', i.e., the whole of India except Jammu and Kashmir. Such service alone is 'taxable service' which is defined under Section 65 B (51) to mean that "any service on which service tax is leviable under Section 66B." The net result is that services rendered outside the taxable territory of India would not be a 'taxable service' for the purposes of the Finance Act. This is of utmost significance since the entire Chapter V applies, in terms of Section 64 (3) of the Finance Act only to "taxable services provided on or after the commencement of this Chapter."

Contentions of the Petitioner

- The Petitioner stated that as a representative of Indian tour operators it had made a representation dated May 22, 2012 to the Joint Secretary, Tax Research Unit in the Ministry of Finance seeking exemption to the tour operators under the amended provisions based on foreign exchange earnings. *Inter alia* it was contended that the principle of Export of

Services cannot be changed year after year and that it should be defined through legislation by the Parliament and not by the Rules. Since tour operators were earning huge foreign exchange for the country, they ought to be given the status of exporters of service.

- The Petitioners also pointed out that although payments were received in convertible foreign exchange, the members of the Petitioner Association did not get the benefit of exports since the place of provision of service was treated as India.
- According to the Petitioners, the action of the Respondent adversely affected the interests of tour operators as they had to suffer huge service tax liability without being extended the benefit of 'Export of Service'.
- The Petitioner also contended that there was an anomalous situation being created, where provision of package tour services to foreign tourists outside India, for instance, in the neighboring countries, were also sought to be taxed in India. The Petitioner further referred to the case of *Cox & Kings India Limited v. Commissioner*[1], where it was held by the Customs, Excise and Service Tax Appellate Tribunal that service tax cannot be levied with regard to outbound tours arranged for Indians by the Indian tour operators since it was a service provided outside the taxable territory of India.
- The Central Thrust of the submission of the Petitioner is that Rule 6A suffers from the vice of excessive delegation. This is because non-taxable services such as services provided outside the taxable territory to foreign tourists, are sought to be brought within the ambit of service tax. Reference is made to the twin cases of *Union of India vs S. Srinivasan* and *General Officer Commanding-in-chief vs Subhash Chandra Yadav*. The Petitioner further pointed out that Section 94 (2) (f) of the Finance Act enabled the Central Government to make rules only for determining export of taxable services. No tax thereon could be levied by the Central Government in terms of the said provision. That was an essential legislative function which could not have been delegated to the Central Government. If Section 94 (2) (f) of the Finance Act too would be vulnerable to invalidation on the ground that it was *ultra vires* the Finance Act. As a result of having to pay service tax, which had to be passed on to the customers, i.e., foreign tourists, the Indian tour operators were losing business to their foreign counterparts. Thus, Rule 6A was arbitrary, discriminatory and violative of Articles 14 and 19 (1) (g) of the Constitution of India.

Contentions of behalf of the Respondents

- The Respondents contented that in terms of Section 94 (1) of the Finance Act, it was permissible for the Central Government to make rules as long as they were consistent with the object and purpose of the Finance Act. Relying on the cases of *Pratap Chandra Mehta*

[1] 2014 (35) STR 817 (Tri-Del)

vs State Bar Council of Madhya Pradesh, and *Kunj Behari Lal Butail vs State of Himachal Pradesh*, the Respondents maintained that Rule 6A of the ST Rules was validly made in terms of the power granted to the Central Government under Section 94 (2) (f) of the Finance Act.

- The Respondents did not dispute that the services provided outside the taxable territory cannot be made amenable to service tax under Section 66B of the Finance Act. He submitted that other than Section 66B, the Central Government could make rules for determining the place of provision of services. Rule 9 of the PPSR 2012 read with Rule 6A of the ST Rules permitted levy of service tax since the service to the foreign tourist was provided in India by the tour operator located in India.
- The Respondents further submitted that under Section 93A of the Finance Act, rebate was granted in cases 'where any goods or services are exported.' Section 93B of the Finance Act stated that all rules made under Section 94 and applicable to the taxable services shall also be applicable to any other service insofar as they are relevant to the determination of any tax liability, refund, credit of service tax or duties paid on inputs and input services or for carrying out the provisions of Chapter V of the Finance Act.

Judgment

- Rule 6A (1) read with Section 6A (2) of the ST Rules, insofar as it seeks to describe export of tour operator services to include non-taxable services provided by tour operators, is *ultra vires* the Finance Act and in particular Section 94 (2) (f) of the Finance Act and is, therefore, invalid.
- Section 94 (2) (f) or (hhh) of the Finance Act does not empower the Central Government to decide taxability of the tour operator services provided outside the taxable territory. They only enable the Central Government to determine what constitutes export of service, the date for determination of the rate of service or the place of provision of taxable service.
- Section 66 C of the Finance Act enables the Central Government only to make rules to determine the place of provision of taxable service but not non-taxable service.
- The net result is that the services provided by Indian tour operators to foreign tourists during the period from July 1, 2012 to July 1, 2017, which has been paid for in convertible foreign exchange would not be amenable to service tax.

Court should apply the principle of prospective overruling so that the Central Government does not have to refund the Service Tax collected on the services provided by Indian tour operators to foreign tourists. This Court would only like to observe that if as a result of this judgment any service tax becomes refundable, the claim for refund will be processed and paid in terms of the extant provisions of the Finance Act read with the Central Excise Act 1944 and the rules thereunder.

S.S. RANA & CO.

ADVOCATES

317, Lawyers Chambers, High Court Delhi, New Delhi 11000. India
t: 91-11 - 3056 2000, 2338 4491 f: 91-11 -3056 2010, 2338 6201 e: ssrana@ssrana.com
w: www.ssrana.com