

**CUSTOMS, EXCISE & SERVICE TAX APPELLATE TRIBUNAL
CHENNAI**

REGIONAL BENCH

SERVICE TAX APPEAL NO. 40052 OF 2019

(Arising out of Order-in-Appeal No. 158/2018 dated 04.10.2018 passed by Commissioner (Appeals) of GST and Central Excise, Salem)

**M/s. Steel Authority of India
Ltd., Salem**

...Appellant

VERSUS

**Commissioner of GST &
Central Excise, Salem**

...Respondent

APPEARANCE:

Ms. Krithika Jaganathan, Advocate for the Appellant
Shri Balakumar and Shri L. Nandakumar Authorized Representatives of the
Department

**CORAM: HON'BLE MR. JUSTICE DILIP GUPTA, PRESIDENT
HON'BLE MR. P.V. SUBBA RAO, MEMBER (TECHNICAL)**

**Date of Hearing: July 20, 2021
Date of Decision: July 26, 2021**

FINAL ORDER No. 41707 / 2021

JUSTICE DILIP GUPTA:

M/s. Steel Authority of India Limited, Salem¹, which is a Public Sector Undertaking engaged in the manufacture of carbon steel, carbon steel sheet, coin blanks and alloy steel has sought the quashing of the order dated 04.10.2018 passed by the Commissioner (Appeals), by which the order dated 15.11.2017 passed by the Assistant Commissioner has been upheld and the appeal has been dismissed.

2. The period involved in all the appeal is after 01.07.2012 and the case set out by the Department is that the appellant had agreed to tolerate breach of timelines stipulated in the contract; the amount imposed as liquidated damages are consideration for the act of

1 the appellant

tolerating contractual default; and that the appellant had rendered declared service of 'agreeing to the obligation to refrain from an act, or to tolerate an act or a situation or to do an act' contemplated under section 66E(e) of the Finance Act, 1994².

3. The following amounts have been alleged as consideration for "agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act" under section 66E(e) of the Finance Act.

Amount sought to be taxed	Description of transaction	Clauses of Contract
Liquidated damages	Liquidated damages are exacted for failure to deliver consignments within the delivery schedule	Clause 11 - General Conditions of Contract;
Forfeiture of EMD	Earnest Money Deposit is forfeited on failure of the successful bidders to make full payment within the date specified in the sale order	Clause 16 - Conditions for sale through Online Forward Auction
Ground Rent	Ground Rent is recovered for extension of due date for payment of Full Sale Value at a cost of Rs. 500 per lot for every day of, extension agreed.	

4. As the timelimits mentioned in the contract were not adhered to, the appellant recovered liquidated damages as per the clauses of the contract.

5. A show cause notice dated 17.04.2017 was issued to the appellant calling upon the appellant to show cause notice as to why:

- "i) the provision to Section 73(1) of the Finance Act 1994 should not be invoked to demand service tax beyond the normal period.
- ii) the service tax amounting to Rs. 2768760/-, EC Rs. 45539/-, SHEC Rs 22769/- SBC Rs 5241/- totaling Rs. 2842309/- - (Rupees twenty eight lakhs forty two thousand three hundred and nine only) as detailed in annexure to the notice payable on the said service provided by them for the period 01.07.2012 to 30.12.2015 should not be demanded from them under proviso to Section 73(1) of the Finance Act, 1994;"

- iii) the applicable interest at the applicable rates should not be recovered from them under Section 75 of the Finance Act 1994 on the Service Tax amount as mention in (ii) above;
- iv) Penalty should not be imposed on them under Section 78 *ibid.*”

6. The appellant submitted a detailed reply dated 18.07.2017 to the aforesaid show cause notice with a request that the proceedings may be dropped for the reason that no service tax was payable on liquidated damages and penalties recovered under the contract.

7. The Assistant Commissioner, however, did not accept the contentions of the appellant and confirmed the demand of service tax by invoking the extended period of limitation contemplated under the proviso to section 73(1) of the Finance Act with interest and penalty.

8. Feeling aggrieved, the appellant filed an appeal before the Commissioner (Appeals) who by order dated 04.10.2018 upheld the order passed by the Assistant Commissioner and dismissed the appeal. The relevant portion of the order passed by the Commissioner (Appeals) is reproduced below:

“05. I have carefully gone through the facts of the case, grounds of appeal, oral and written submissions during Personal Hearing and the provisions of law relating to the subject issue. The gist of the appeal is that whenever the suppliers defaulted in adhering to the time schedule prescribed by the appellant, recovered (i) liquidated damages @1%. The appellant also sells goods through Online Forward Auction (OFV). The Bidders who intend to purchase goods through OFV, has to pay EMD as prescribed in the notice. A permanent customer as well as temporary customer is required to pay certain amount as EMD for every auction they intend to participate. The successful bidder has to pay 10% of the bid value towards Additional Security Deposit (ASD) and Full Sale Value (FSV) as per sale order. In the event of failure on the part of the successful bidder to make ASD/FSV payments within the due date as stipulated in the Sale Order, (ii) the EMD shall forfeited. In the OFA transaction, the appellant permits extension of time for payment of the FSV for a period not exceeding 3 days on payment of specified amount for every day of extension. This amount is termed as (iii) Ground Rent. The department contended that the amount recovered by the appellant for non-fulfilment of obligation in terms of the agreement under (i), (ii) and (iii) as stated above from their suppliers and buyers(bidders) are nothing but consideration for tolerating an act of their customers or a situation and hence the activity is a ‘declared service’ as stated under

Section 66E(e) of the Finance Act, 1994 and therefore liable to pay service tax and accordingly confirmed the demand of service tax against which present appeal filed.”

9. Ms. Krithika Jaganathan, Learned counsel appearing for the appellant in all the five appeals made the following submissions:

- (i) A similar issue concerning service tax liability on liquidated damages has been decided in favour of the appellant in **M/s South Eastern Coalfields Ltd. vs. Commissioner of Central Excise and Service Tax, Raipur³**;
- (ii) Reliance has also been placed on the decision of the Tribunal **M.P. Poorva Kshetra Vidyut Vitran Co. Ltd. vs. Principal Commissioner CGST & Central Excise Bhopal⁴**, in support of the contention that the amount of liquidated damages/penalty collected for non-compliance of the terms of the contracts cannot be subjected to levy of service tax; and
- (iii) Reliance has also been placed on a Larger Bench decision of the Tribunal in **Commissioner of Service Tax, Chennai vs. REPCO Home Finance Ltd.⁵**, wherein it has been held that ‘foreclosure charges’ collected by banks from borrowers for premature closure of loan account are not ‘consideration’ for banking services as foreclosure charges are ‘damages’ collected for breach of terms and conditions in the loan agreement and cannot be construed as ‘consideration’ for banking and other financial services.

10. Shri Balakumar and Shri L. NandKumar learned Authorized Representatives appearing for the Department have, however, supported the impugned orders and have submitted that they do not call for any interference as the demands have been confirmed in accordance with the provisions of section 66E(e) of the Finance Act.

3 2020 (12) TMI 912 – CESTAT NEW DELHI
4 2021 (2) TMI 821 – CESTAT NEW DELHI
5 2020 (42) G.S.T.L. 104 (Tri. –LB)

11. The submissions advanced by the learned counsel for the appellant and the learned Authorized Representatives of the Department have been considered.

12. There is substance in the submission advanced by the learned counsel for the appellant that no service tax is payable on the amount collected towards liquidated damages as this issue has been decided by the Tribunal in favour of the appellant in **South Eastern Coalfields.**

13. Various commercial contracts had been executed by South Eastern Coalfields and certain clause provided for levy of penalty for non-observance / breach of the terms of the contract. A show cause notice was issued with an allegation that the amount charged by the appellant during the period from July 2012 to March 2016 appeared to be taxable as a 'declared services' under section 66E(e) of the Finance Act.

14. The Principal Commissioner, however, did not accept the contention advanced on behalf of the appellant and confirmed the demand of service tax holding that the amount received by the said appellant towards penalty, earnest money deposit forfeiture and liquidated damages would tantamount to a consideration "for tolerating an act" on the part of the buyers of coal/contractors, for which service tax would be levied under section 66 E(e) of the Finance Act.

15. The Tribunal rejected the contentions advanced on behalf of the Department that penalty amount, forfeiture of earnest money deposit and liquidated damages had been received by the said appellant towards "consideration" for "tolerating an act" leviable to service tax under section 66E(e) of the Finance Act.

16. In this connection it would be appropriate to reproduce the relevant portions of the decision of the Tribunal in **South Eastern Coalfields** and they are as follows:

“25. It is in the light of what has been stated above that the provisions of section 66E(e) have to be analyzed. Section 65B(44) defines **service** to mean any activity carried out by a person for another for consideration and includes a declared service. One of the declared services contemplated under section 66E is a service contemplated under clause (e) which service is agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act. There has, therefore, to be a flow of consideration from one person to another when one person agrees to the obligation to refrain from an act, or to tolerate an act, or a situation, or to do an act. In other words, the agreement should not only specify the activity to be carried out by a person for another person but should specify the:

- (i) consideration for agreeing to the obligation to refrain from an act; or
- (ii) consideration for agreeing to tolerate an act or a situation; or
- (iii) consideration to do an act.

26. Thus, a service conceived in an agreement where one person, for a consideration, agrees to an obligation to refrain from an act, would be a ‘declared service’ under section 66E(e) read with section 65B (44) and would be taxable under section 68 at the rate specified in section 66B. Likewise, there can be services conceived in agreements in relation to the other two activities referred to in section 66E(e).

27. It is trite that an agreement has to be read as a whole so as to gather the intention of the parties. The intention of the appellant and the parties was for supply of coal; for supply of goods; and for availing various types of services. The consideration contemplated under the agreements was for such supply of coal, materials or for availing various types of services. The intention of the parties certainly was not for flouting the terms of the agreement so that the penal clauses get attracted. The penal clauses are in the nature of providing a safeguard to the commercial interest of the appellant and it cannot, by any stretch of imagination, be said that recovering any sum by invoking the penalty clauses is the reason behind the execution of the contract for an agreed consideration. It is not the intention of the appellant to impose any penalty upon the other party nor is it the intention of the other party to get penalized.

28. It also needs to be noted that section 65B(44) defines “service” to mean any activity carried out by a person for another for consideration. Explanation (a) to section 67 provides that “consideration” includes any amount that is payable for the taxable services provided or to be provided. The recovery of liquidated damages/penalty from other party cannot be said to be towards any service per se, since neither the appellant is carrying on any activity to receive compensation nor can there be any

intention of the other party to breach or violate the contract and suffer a loss. The purpose of imposing compensation or penalty is to ensure that the defaulting act is not undertaken or repeated and the same cannot be said to be towards toleration of the defaulting party. The expectation of the appellant is that the other party complies with the terms of the contract and a penalty is imposed only if there is non-compliance.

29. The situation would have been different if the party purchasing coal had an option to purchase coal from 'A' or from 'B' and if in such a situation 'A' and 'B' enter into an agreement that 'A' would not supply coal to the appellant provided 'B' paid some amount to it, then in such a case, it can be said that the activity may result in a deemed service contemplated under section 66E (e).

30. The activities, therefore, that are contemplated under section 66E (e), when one party agrees to refrain from an act, or to tolerate an act or a situation, or to do an act, are activities where the agreement specifically refers to such an activity and there is a flow of consideration for this activity."

17. This decision of the Tribunal in **South Eastern Coalfields** was followed by the Tribunal in **M.P. Poorva Kshetra Vidyut Vitran**.

18. In view of the aforesaid decisions of the Tribunal, it is not possible to sustain the view taken by the Commissioner that since the task was not completed within the time schedule, the appellant agreed to tolerate the same for a consideration in the form of liquidated damages, which would be subjected to service tax under section 66E(e) of the Finance Act.

19. As service tax could not be levied, the imposition of interest and penalty also cannot be sustained.

20. Thus, for all the reasons stated above, the order dated 04.10.2018 passed by the Commissioner (Appeals) is set aside and the appeal is allowed.

(Order pronounced on 26.07.2021)

(JUSTICE DILIP GUPTA)
PRESIDENT

(P V SUBBA RAO)
MEMBER (TECHNICAL)