2023 INSC 711

Non-Reportable

IN THE SUPREME COURT OF INDIA
CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO.4007 OF 2019

Commissioner of Service Tax, Mumbai-II ... Appellant

versus

M/s 3I Infotech Ltd. ... Respondent

with

Civil Appeal No.7155 OF 2019

M/s 3I Infotech Ltd. ... Appellant

versus

Commissioner of Service Tax, Mumbai ... Respondent

J U D G M E N T

ABHAY S. OKA, J.

FACTUAL ASPECTS

1. These two appeals arise out of service tax demands on the basis of four Show Cause Notices. The notices

were issued under Section 73 of the Finance Act, 1994 (for short "the Finance Act") for the demand of service tax. The brief particulars of Show Cause Notices are as under:

Show Cause Notice Date	Period	Demand under Taxable Service
19/10/2009	1.4.2004 to 31.3.2009	Maintenance & Repair
20/10/2010	1.4.2009 to 31.3.2010	Information Technology Software
21/10/2011	1.4.2010 to 31.3.2011	Information Technology Software
22/10/2012	1.4.2011 to 31.3.2012	Information Technology Software

2. The adjudication in respect of Show Cause Notices was made by the Commissioner which was challenged before the Customs, Excise and Service Tax Appellate Tribunal, West Zonal Bench at Mumbai (CESTAT). An order of remand was passed by CESTAT. In the order of remand, CESTAT observed that it is not borne out from the impugned order of the Commissioner how service tax

liability has been computed. CESTAT further observed that if the assessee has purchased software from third parties and sold the same on payment of VAT and supplied hardware on payment of VAT, the same would not be liable to service tax. It was further held that the liability to service tax would arise only in respect of the software which the assessee has developed as per customers' specifications and supplied to their customers. The Tribunal further observed that it was necessary to go through the agreements entered into by the assessee with his clients, bills raised for services rendered, the goods supplied and the payments made towards the service tax liability.

3. On the basis of the order of remand, the Commissioner of Service Tax, Mumbai-II made adjudication on the four Show Cause Notices. The Commissioner held that the services rendered by the assessee from 10th April 2004 up to 15th May 2008 in relation to software need to be classified under the

category of "Intellectual Property Service" defined under Section 65 (55b) of the Finance Act. It was further held that from 16th May 2008 onwards, in relation to the software, the classification of service rendered should be under the category of "Information Technology Software" defined under Section 65 (53a) of the Finance Act. Thirdly, it was held that the value of the computer hardware items consumed for providing the services is required to be included in the valuation of the respective services in terms of Section 67 of the Finance Act. Consequential orders regarding payment of interest and penalty were passed by the Commissioner.

4. Being aggrieved by the said Order-in-Original, the assessee preferred an appeal before the CESTAT. By the impugned judgment dated 18th September 2018, CESTAT held that the services subject matter of dispute were classifiable under the category of "Information Technology Software" with effect from 16th May 2008 and for the earlier period up to 15th May 2008, the same

services were classifiable under the category of "Intellectual Property Service". The Tribunal held that the show cause notice dated 19th October 2019 covering the period up to 16th May 2008 was not justified. However, the Tribunal, for the period on and after 16th May 2008 passed a limited order of remand.

5. Civil Appeal No. 4007 of 2019 has been preferred by the Revenue against the same order and Civil Appeal No. 7155 of 2019 has been filed by the assessee.

SUBMISSIONS

6. In support of Civil Appeal No.4007 of 2019, learned ASG, Shri Mr N.Venkatraman submitted that though the first show cause notice dated 19th October 2009 has been issued demanding service tax under the category of "Management, Maintenance and Repairs", the assessee was always aware that in fact the demand was covered under the category "Intellectual Property Service". He urged that in any case, only a part of the demand under the first show cause notice up to 15th May 2008 could

have been held to be illegal and not for the subsequent period. The learned counsel appearing for the assessee supported the finding of CESTAT on the first show cause notice.

7. The learned counsel appearing for the assessee in support of its appeal firstly urged that by the judgment of CESTAT dated 14th January 2013, it was held that the software purchased by the assessee from third parties and sold the same on payment of VAT and the hardware sold on payment of VAT will not be subject to service tax. Secondly, as regards the finding recorded in paragraph no.10.16 of the impugned judgment regarding exemption in respect of supplies to a developer or unit in SEZ, he urged that in view of sub-section (2) of Section 26 of Special Economic Zones Act, 2005 (for short, 'SEZ Act'), an exemption was available in the light of what is provided in the Special Economic Zone Rules, 2006 (for short, 'SEZ Rules'). He submitted that in view of the availability of exemption, the finding of the CESTAT that

the assessee was required to pay service tax and thereafter, SEZ developer or unit located in SEZ could have claimed the exemption by way of refund, is completely erroneous. The learned counsel appearing for the assessee thirdly submitted that on the same point, there is a decision of the High Court of Judicature at Hyderabad in the case of ***GMR Aerospace Engineering Limited, and Another v. Union of India, through the Secretary, Ministry of Commerce and others***[1] rendered on 27th December 2018 which has been confirmed by this Court on 26th July 2019 in SLP (Civil) Dy.No. 22140 of 2019. He pointed out that based on the said decision, this Court dismissed Civil Appeal No. 549 of 2023 against judgment and order dated 1st September 2022 in Service Tax Appeal No. 86312 of 2018 preferred by the present appellant before CESTAT.

8. The learned counsel appearing for the assessee submitted that CESTAT committed an error in upholding

1 2018 SCC OnLine Hyd 767

the demand confirmed by the respondent for the period from 16th May 2008 on the sale of standardised software and resale of the hardware.

OUR VIEW

APPEAL OF REVENUE

9. We have given careful consideration to the submissions. Firstly, we deal with the appeal preferred by the Revenue. The appeal is confined to the first show cause notice. The first show cause notice covers the period from 1st April 2004 to 31st March 2009. The demand under the said show cause notice dated 19th October 2009 was for taxable service of "Management, Maintenance and Repair". The CESTAT found that the service of transfer of intellectual property rights was classifiable under the category of "Intellectual Property Service" till 16th May 2008 and was taxable in terms of Section 65(105)(zzr) of the Finance Act. In the Union Budget of 2008-09, a new service under the head "Information Technology Software" was defined separately

under Section 65(53a) of the Finance Act. The said service was made taxable in terms of Section 65(105)(zzzze). Thus, the transfer of the right to use the software was covered by the service classifiable as "Information Technology Software" with effect from 16th May 2008. In fact, the CESTAT relied upon the clarification given by CBEC by Circular dated 29th February 2008 which clarifies the position, as stated above.

10. It is pertinent to note here that the first show cause notice dated 19th October 2009 contained a demand for service tax under the taxable service of "Management, Maintenance and Repair" and the rest of the three notices contain a demand under classifiable service "Information Technology Software". In the facts of the case, the demand was made on account of services provided by the assessee in respect of the supply of third-party software, software developed in-house or customised software. The assessee had temporarily transferred the right to use the said software to their clients. Thus, prior to 16th May

2008, such service was classifiable under the category of "Intellectual Property Service" and with effect from 16th May 2008, it was classifiable under the category of 'Information Technology Software". In fact, the management, maintenance and repair services of computer hardware as well as software under the annual maintenance contract was covered by the category of "Management, Maintenance or Repair" services which was defined under Section 65(64) of the Finance Act. Thus, the classification mentioned in the first show cause notice was completely erroneous. Therefore, CESTAT was right in holding that the first show cause was illegal. Elementary principles of natural justice required that the adjudication on the basis of show cause notice should be made only on the basis of classification stated in the show cause notice. Assessee cannot be subjected to a penalty on the basis of a show cause notice containing a completely erroneous category of service. Therefore, the demand made on the basis of the first show cause notice

was illegal. Therefore, we find that there is no merit in the appeal preferred by Revenue.

APPEAL OF ASSESSEE

11. Now, we come to the other three show-cause notices. We have carefully perused the findings recorded by CESTAT. As stated earlier, the other three show-cause notices mentioned the correct classification. Reliance is placed on the earlier order of remand passed by CESTAT. However, we find that said order of remand does not decide any issue on merits and therefore, after the remand, the issue was wide open. The issue to be considered was whether in respect of the particular transactions, service tax was payable under the classification mentioned in the show cause notices. After having perused the findings of CESTAT, we find that the findings rendered by the Tribunal call for no interference. The findings are based on careful consideration of the factual and legal aspects.

12. In paragraph no. 10.16, CESTAT dealt with the argument that an exemption was available to the assessee under SEZ Act in respect of services supplied to SEZ units. Sub-section (2) of Section 26 of SEZ Act provides that the Central Government may prescribe the manner in which and the terms and conditions subject to which exemptions shall be granted to a developer or entrepreneur covered by sub-section (1) of Section 26. Clause (e) of sub-section (1) of Section 26 refers to exemption from service tax under the Finance Act on taxable services provided to a developer or unit to carry on authorised operations in SEZ. Under Sub-section (1) of Section 51, SEZ Act prevails over other enactments which are inconsistent to the provisions contained therein. Thus, only when by exercising the power under sub-section (2) of Section 26 of SEZ Act, an exemption is granted by the Central Government that the assessee can claim exemption. Otherwise, the exemption notification referred in paragraph 10.16 will apply.

13. On this issue, the CESTAT held thus:-

> "In terms of Notification No. 9/2009-ST granted exemption to the specific services supplied to SEZ subject to condition that person liable to pay service tax shall pay service tax as applicable on the specified services provided to the developer or units of SEZ and SEZ shall claim refund of service tax on the services provided to the developer of SEZ. Notification No. 9/2009-S.T was substituted by Notification 17-2011-ST which provided exemption from service tax subject to condition specified therein. One of the conditions specified was that the exemption shall be provided by way of refund of service tax. Accordingly, during the entire period the service provider is not eligible for first stage exemption from payment of service tax. He was required to pay service tax and either SEZ developer or unit located in SEZ could have claimed the exemption by way of refund of service tax. Further in the present case, appellant has not produced any evidence to show that the services provided by them or only or partly consumed within the SEZ or outside. Thus, there is no dispute about the fact that said exemption or not available to the appellant during the relevant period. Since Commissioner has not considered the matter on this aspect the issue needs to be remanded

> back to him for consideration of the exemption in respect of services supplied to SEZ unit/developer."

14. Therefore, we cannot find fault with the reasoning adopted by CESTAT. However, in the proceedings pursuant to remand, it will be open for the assessee to show that an exemption was available under sub-section (2) of Section 26 of the SEZ Act.

15. In paragraph 10.17, it was held that octroi charges are in the nature of levy for transportation of goods. Therefore, octroi charges cannot be a part of the value of the taxable services. However, a remand was ordered to enable the assessee to produce evidence regarding the amounts paid towards octroi charges.

16. After having perused the entire judgment of CESTAT and the Commissioner, we find that except for the clarification that we have issued in paragraph 14 above as regards paragraph no.10.16, no other interference is called for.

17. Accordingly, we pass the following order:

a. Civil Appeal No. 4007 of 2019 is dismissed;

b. Civil appeal No. 7155 of 2019 is also dismissed subject to the clarification made to paragraph no.10.16; and

c. There will be no order as to costs.

.....J.
(Abhay S. Oka)

.....J.
(Sanjay Karol)

New Delhi;
August 14, 2023.