Business Auxiliary Services: Some Issues

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Business Auxiliary Services fall in one of the 'Controversial Services Category'. Drafting of the clauses in the statutory definition/terminology employed is capable of very wide interpretations. Government Clarifications have added to the confusion rather than providing clarity. There is significant uncertainty, as to the scope of the Service Category amongst the Service Providers at large. Divergent views expressed by professionals have increased the uncertainty. This article discusses some of such important issues. The same needs to be speedily addressed to avoid extensive litigations.

The relevant extracts of the Finance Act, 1994 (as amended from time to time up to Finance Act, 2005) ["Act"] pertaining to Business Auxiliary Service (BAS) are set out hereafter for ready reference:

Section 65 (19) of the ("Act")

Business Auxiliary Service means any service in relation to: -

(i) Promotion or marketing or sale of goods produced or provided by or belonging to the client; or

(ii) Promotion or marketing of service provided by the client; or

(iii) Any customer care service provided on behalf of the client; or

(iv) Procurement of goods or services, which are inputs for the client; or

'Explanation – For the removal of doubts, it is hereby declared that for the purposes of this sub-clause, "inputs" means all goods or services intended for use by the client,'

(v) Production of goods for or on behalf of the client; or

(vi) Provision of service on behalf of the client; or

(vii) A service incidental or auxiliary to any activity specified in sub-clauses (i) to (vi), such as billing, issue or collection or recovery of cheques, payments, maintenance of accounts and remittance, inventory management, evaluation or development of prospective customer or vendor, public relation services, management or supervision and includes services as a commission agent, but does not include any information technology service and any activity that amounts to "manufacture" within the meaning of clause (f) of section 2 of the Central Excise Act, 1944 (1 of 1944).

'Explanation – For the removal of doubts, it is hereby declared that for the purposes of this clause-

(a) "Commission Agent" means any person who acts on behalf of another person and causes sale or purchase of goods, or provision or receipt of services, for a consideration, and includes any person who, while acting on behalf of another person –

(i) deals with goods or services or documents of title to such goods or services, or

(ii) collects payment of sale price of such goods or services; or

(iii) guarantees for collection or payment for such goods or services; or

(iv) undertakes any activities relating to such sale or purchase of such goods or services;

(b) "Information Technology Service" means any service in relation to designing, developing or maintaining of computer software, or computerised data processing or system networking, or any other service primarily in relation to operation of computer systems;

Section 65 (105) of the Act

Taxable Service means any service provided or to be provided -

(zzb) to a client, by a commercial concern in relation to business auxiliary service.

Overall scope and ambit

a) A close perusal of statutory definition of BAS is indicative of the following terminology being employed viz:

- Any service in relation to
- Provision of service on behalf of the client [Sub – Clause (vi)]
- A service incidental or auxiliary to any activity [specified in Sub – clauses (i) to (vi)]

The above can be collectively interpreted to indicate a very wide connotation as to the overall scope and ambit of BAS.

In an important ruling under Service Tax, *viz Tamil Nadu Kalyanaa Mandapam Assn. v. UOI (2004) 167 ELT 3(SC)*, wide connotation of the phrase "in relation to" has been confirmed by the Supreme Court [Reliance was placed on *Doypack System (P) Ltd. v. UOI (1988) 2 SCC299; Renu Sagar Power Co. Ltd. (1984) 4 SCC 679 and Steel Authority of India Ltd. (1999) 9 SCC 334.]*

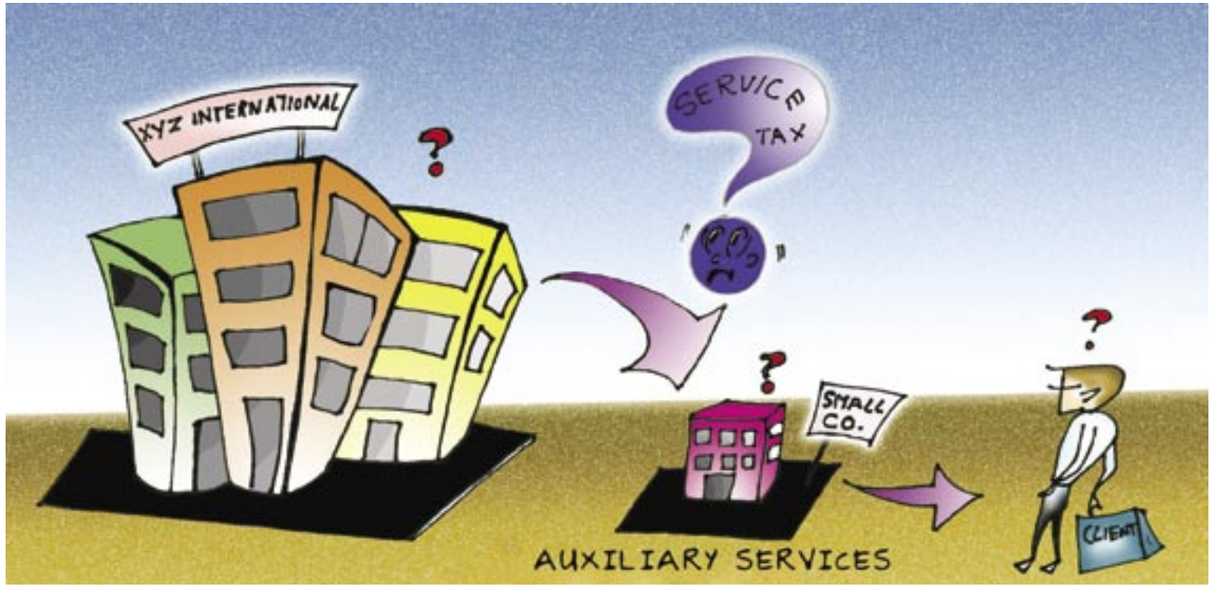
In view of the foregoing, an important issue that arises for consideration is, whether scope of BAS is wide enough so as to cover all services which are otherwise not classifiable under any other taxable services specified u/s 65 (105) of the Act.

If BAS is construed as an omnibus Service Category like [erstwhile Tariff Item 68 under Central Excise], it could result in absurd situations, whereby even lawyers and doctors could become liable to Service Tax.

Considering, the evolution of Services Categories since introduction of Service Tax, substantial expansion in scope existing Services Categories from time to time and harmonious construction of Service Tax legislation, it would reasonably appear that, though terminology employed in BAS definition is capable of wide interpretations, a better and more appropriate view would be that, overall scope and ambit of BAS is restrictive and not of widest amplitude so as to cover even services which are not classifiable under any taxable Services Categories u/s 65 (105) of the Act.

b) An incidental issue that arises for consideration is, whether persons who provide services similar to Sub – Brokers viz Authorised Persons/ Remisiers but are not registered with SEBI, could be made liable to Service Tax under BAS under clauses (i), (vi)/ or as Commission Agents.

It would appear that on an application of Services Classi-



fication Rules (viz Section 65A of the Act) appropriate Classification of the aforesaid services would be "Stock Broker Services". However, since the said persons are not registered with SEBI, they are not liable to Service Tax under "Stock Broker Services". Hence they cannot be made liable to Service Tax under any other General Category viz BAS.

The above view is further substantiated by Settled Principle of Commodities Classification laid down by the Apex Court to the effect that Specific Classification would prevail over General Classification *[Ref: SCE v. Vac Met Corporation Pvt. Ltd 22 ELT 330 (SC); CCE v. Jayant Oil Mills Pvt. Ltd. 40 ELT 287 (SC); Plasmae Machine Mfg Co. Pvt Ltd. v. CCE 51 ELT 161 (SC); Moorco (India) Ltd. v. CC 74 ELT 5 (SC); Speedmax Rubber Co v. CCE 143 ELT 8 (SC)]*

Commercial concern

In order to be made liable to Service Tax under BAS, it is essential that, service provider must be a "Commercial Concern". However, the said term has not been defined under the Act. Hence issues arise as to what is a "Commercial Concern" for the purpose of BAS.

Various meanings attributed in Dictionaries,/Judicial Pronouncements/Department Clarifications etc., in regard to "Commercial Concern" are analysed hereafter:

- *Concise Oxford Dictionary:*

"Commercial' means of, engaged in, or connected with, commerce' or 'having profit as a primary aim rather than artistic etc. value'. 'Concern' means 'a business, a firm'. 'Firm' means 'business concern' or 'a group of persons working together"

- *Black's Law Dictionary*:

"Commercial" relates to or is connected with trade and traffic or commerce in general; is occupied with business and commerce. Generic term for most/all aspects of buying and selling.

- *Sakharam Narayan Khedekar vs. City of Nagpur Corporation AIR 1964 Bom. 200.*

"Commercial activity must imply some investment of capital and the activity must run the risk of profit or loss relating to or connected with trade and traffic or commerce in general"

- *Laxmi Engineering Works v. P.S.G. Industrial Institute [1995AIR SCW 2114; AIR 1995 SC 1428; (1995) 3 SCC 583 = (1995)]*

'Commercial' means 'connected with or engaged in commerce having profit as the main aim'. [The issue was under "Consumer Protection Act'. As per that Act, a person purchasing goods for commercial purpose is not a 'consumer'. In this case, it was held that any person buying goods for purpose of being used in any activity on a large scale for making profit is not a 'consumer'].

- *CBE&C circular No. 62/11/2003 – ST dated 21-8-2003:*

Services provided by individual will be exempt from service tax on erection, commissioning and installation services, as he is not 'commercial concern' [reiterated in Directorate of Publicity, Customs & CE October 2003 publication Q 11.1 158 ELT T23 = 134 Taxman 25 (Stat.)]

- *MF(DR) circular No. B2/8/2004-TRU dated 10.9.2004:*

In the context of construction service 'the tax is limited only in case the service is provided by a commercial concern. Thus service provided by a labourer engaged directly by the property owner or a contractor who does not have a business establishment would not be subject to service tax'.

- In *V.K. Thampi v. CCE&CE – 1998 (33) ELT 424 [CEGAT] – quoted with approval in Pragati Press v. CC 1994 (72) ELT 620 [CEGAT) and Goyal Tin Works (P.) Ltd. v. CCE 1995 (78) ELT 316 [CEGAT]*, it was held that both proprietor and proprietary firm cannot be subjected to penalty at the same time for same cause of action, as both are same.

If BAS is construed as an omnibus Service Category like [erstwhile Tariff Item 68 under Central Excise], it could result in absurd situations, whereby even lawyers and doctors could become liable to Service Tax

From the foregoing analysis, the following essential characteristics emerge for a person to be treated as 'Commercial Concern'.

- The person concerned must be a business organisation with an establishment necessary for conduct of relevant business. The same may be Sole Proprietorship, Partnership, HUF, Company, Pvt. Trust etc.
- There must be profit motive in contrast to Charitable Institutions, Educational Institutions, etc. who do not have any profit motive to conduct its activities. It is essential that the purpose of carrying out the relevant activity should primarily and necessarily be to earn profit.

Interpretation of "on behalf of"

(a) The words 'on behalf of' are employed in Section 65 (19) of the Act in various clauses are very important in the definition. Hence, issue arises as to, what would constitute "on behalf of".

The various meanings attributed to "on behalf of" are as under:

- 'On behalf of' means (a) In the interests of a person, group, or principal; (b) as a representative of. [*Oxford Concise Dictionary*]
- The expression "on behalf of" connotes some benefit to the person on whose behalf another person acts [39 CAL 344]
- The words 'on behalf of' connote an agency; when one person acts on behalf of other, the former acts as agent of the latter. – *[The State of Mysore v. Gangamma AIR 1965 Mys 235.- Cirminal Procedure Code – Sec 198]*
- The expression 'on behalf of' means that holder of property is only a representative of the real owner – *[Kripa Shankar v. Commissioner of Wealth Tax AIR 1966 Pat. 371.]*
- A contract by certain parties on behalf of others prima facie imports that they made the contract only as agents.

[Law Lexicon – P Ramnatha Aiyar].

(b) One View: On the basis of analysis of "on behalf of" there is one school of thought which suggests that in order to be covered within the relevant of clauses of Section 65 (19) of the Act three parties are contemplated:

- Person who gets the specified work/activity done through others (Supplier)
- A Commercial Concern who carries out the specified work/activity on behalf of the said Supplier.
- A Specific Customer of Supplier for whom the Specified work/activity is carried out by the said Commercial Concern.

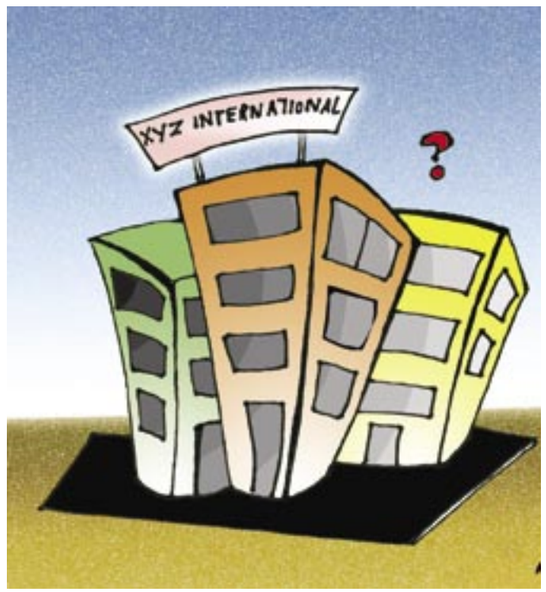
To illustrate: If a Call Centre (say 'A') provides Customer Care services on behalf of B, it actually attends to the problems of the customers of B (say C). Here A would be rendering under the clause (iii). In the situation, B is the client on whose behalf the A is providing services to C. One cannot imagine customer care service being provided on behalf of the client, without presence of a third party viz. C. Further B cannot themselves become a third party. A cannot provide a customer care service to B on behalf of B. The service has necessarily to be provided to a third party who would claim the service from B. By providing the service, A would be discharging its obligation of B towards C.

The expression 'on behalf of' means that the holder of the property is only a representative of the real owner – *[Kripa Shankar v. Commissioner of Wealth Tax AIR 1966 Pat. 371.]*

If A provides customer care service to B themselves, it cannot be said that A provides 'customer care service on behalf of B. A service provided by an agent to the principal himself is not on behalf of the principal. An agent represents his principal to the rest of the world. The agent does not represent his principal to the principal himself.

(c) Second View: Dept. Clarification dated 10.9.04, explaining the scope of expanded Business Auxiliary Services, is clearly indicative of the Government's intention to cover all outsourcing services relating to activities specified under Section 65 (19) of the Act excepting activities which amount to "manufacture" under Central Excise & Information Technology Service.

(d) Overall Views: In view of the foregoing discussions, and in particular specific amendment made in clause



(v) of Section 65 (19) by the Finance Act, 2005 whereby the words "on behalf of" have been substituted by "for or on behalf of", it would be reasonably appear that view stated in para (b) above is a better view.

Job Work Related

a) If any job work/service activity constitutes "Manufacture" under Section 2(f) of the Central Excise Act, 1944 ("CEA") then it would be out of the purview of Business Auxiliary Service liable to Service Tax. Hence the basic conceptual understanding of "Manufacture" under Central Excise would be necessary for determination of liability to Service Tax in regard to job work activities.

In order to attract levy of excise duty under Section 3 of CEA the following basic prerequisites should be satisfied:

- There should be production or manufacture of goods in India
- Such production or manufacture should result in creation of excisable goods, and
- Such excisable goods should be specified in the Schedule to Central Excise Tariff Act, 1985 (CETA)

It is possible that in a given case an activity may amount to "manufacture". However, there may be no payment of excise duty due to various reasons. To illustrate:

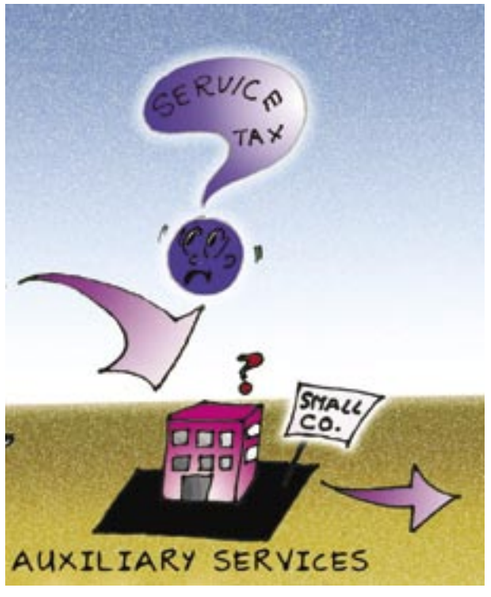
- Activity does not result in creation of excisable goods.
- Activity results in creation of excisable goods. However under CETA there is 'NIL' duty is specified.
- Concerned Manufacturer is operating under SSI Exemption Scheme [NIL duty up to 100 lakhs clearances.]
- Activity is exempted from excise duty under Specific Job Work Exemption Notification.

It needs to be expressly understood that for the purpose of Service Tax it would suffice if an activity amount to manufacture. Aspect of payment of excise duty would not be relevant at all.

The statutory definition of Manufacture under CEA would indicate that "manufacture" under Central Excise has to be construed through a *3TIER Process*:

- "general concept" of manufacture
- "deemed concept" of manufacture
- "MRP concept" of manufacture

(i) The general concept of manufacture has been a subject matter of detailed discussion in a number of cases by the Supreme Court in the context of Central Excise as well as Sales Tax. There are various leading case laws on the subject, which have laid down principles as to what constitutes "manufacture".



(ii) In addition to the general concept of manufacture there is a deeming fiction under Section 2(b) of CEA, which provides that if an activity, in relation to specified Chapter headings/Chapter of CETA, is specified in the relevant Chapter Notes/Section Notes of CETA, then such activity would amount to manufacture and would attract levy of excise duty.

To illustrate: An activity of repacking from a bulk pack to smaller pack would usually not amount to manufacture under the general concept. However, if such an activity is specified under a Chapter Note in relation to specified Chapter/ Chapter headings of CETA then such activity would be deemed to be manufacture and attract levy of Central excise duty, irrespective of the principles relating to manufacture.

(iii) Further in regard to (about 98 products specified in Third Schedule to CETA) which are under MRP based levy, the concept of manufacture, has been extended to cover activities of packing, repacking, labelling, etc.

Hence in order to determine whether any activity amounts to manufacture under, CEA, the 3 Tier process stated above, would have to be gone through.

b) The Central Government has issued Notification No. 8/2005 dated 1.3.2005 exempting the taxable service of production of goods on behalf of the client from service tax subject to the following conditions:

- Goods are produced using raw material or semi-finished goods supplied by the client;
- The goods so produced are returned back to the client for use in or in relation to the manufacture of any other goods on which "appropriate excise duty is payable" i.e. the final product should not be wholly exempt or subject to 'Nil' rate of duty,

In this context the expression "production of goods" means working upon raw materials or semi-finished goods so as to complete part or whole of production, subject to the condition that such production does not amount to "manufacture" within the meaning of Section 2(f) of CEA;

An issue that arises for consideration is, whether the above exemption would be available, in cases where job work is done for a SSI Unit availing 100 lakhs Exemption or for a manufacturer who is otherwise not liable to pay excise duty for any reason.

A close reading of the aforesaid Exemption Notification is clearly indicative that Service Tax Exemption would be available, only in cases where, the job work is done for a manufacturer who is ultimately paying excise duty on the finished product. In all other cases there would be liability to Service Tax unless specifically exempted [eg. Diamond, Jewellery etc. vide Notification No. 19/2005 – ST dated 7.6.05]

Sub–contracted services

An important issue that arises for consideration is, whether Sub-contracted service providers, could be made liable to Service Tax under BAS (Clause vi) w.e.f 10.9.04.

(a) As regards, liability of Sub-contracted Service Providers to Service Tax, though there were no specific provisions under the Act/nor Exemption Notifications were issued, Exemptions were granted through Dept. Trade Notices provided:

- Services Category of the Main Service Provider and Sub – Contracted Service Provider was same; and
- Service Tax was appropriately discharged on the Full Contract at the end of Main Service Provider.

Despite there being no statutory force, the above exemptions were availed by the Service Providers. However, for the period after introduction of Input Credit Mechanism and more particularly after 10.9.04, it is felt that availment of exemptions by Sub-contracted Service Providers in terms of Trade Notices could be disputed by the Service Tax Authorities which could result in litigations.

(b) In case, the Services Category of the Main Service Provider & Sub-contracted Service Provider is different, it is felt that strictly the Trade Notices granting Exemptions stated in would not apply.

(c) In case Service Tax is paid by the Sub-contractors, the Main Contractor would be able to avail Cenvat Credit if the said service constitutes "Input Service" in terms of Cenvat Credit Rules, 2004 and subject to compliance of Specified Conditions there under.

(d) In case, Service Tax Authorities dispute the availment of Exemptions by Sub-contractors based on Dept. Trade Notices, and the matter is finally decided against the Sub-Contractors, they would have to pay Service Tax with interest and penalty, as applicable.
Whether, the Service Tax paid belatedly can be availed as credit by the Main Contractor, could face technical objections by the Authorities, which could again result in litigations. Entitlement to Credit at the end of Main Service Provider would have to be examined under the facts of a given case and conditions under Cenvat Credit Rules, 2004.

(e) For the period after 10.9.04, more particularly after expansion in Scope of BAS [viz clause (vi)], it would be advisable for the Sub-contractors to register themselves and discharge the appropriate Service Tax Liability. The Service Tax so paid can be availed as credit by the Main Service Provider subject to compliance of conditions specified under Cenvat Credit Rules, 2004. ❐