

**CUSTOMS, EXCISE & SERVICE TAX APPELLATE TRIBUNAL
NEW DELHI**

PRINCIPAL BENCH-COURT NO. I

SERVICE TAX APPEAL NO. 52298 OF 2015

[Arising out of Order-in-Order No. 89-90 (SLM)/ ST/ JPR/2015 dated 23.03.2015 passed by the Commissioner, Central Excise (Appeals), Jaipur I]

RAJASTHAN FINANCIAL CORPORATION

APPELLANT

VS.

**ADDL. COMMISSIONER, CENTRAL EXCISE
JAIPUR**

RESPONDENT

APPEARANCE:

Shri S C Kamra & Shri N D Dubey, Advocates for the Appellant
Dr. Radhe Tallo, Authorized Representative for the Department

CORAM:

**HON'BLE MR.JUSTICE DILIP GUPTA, PRESIDENT
HON'BLE MS. HEMAMBIKA R. PRIYA, MEMBER (TECHNICAL)**

**DATE OF HEARING : 01 February, 2023
DATE OF DECISION : 13 March, 2023**

FINAL ORDER No. 50303/2023

PER HEMAMBIKA R PRIYA

This appeal has been filed to assail the order No. 89-90 (SLM)/ ST/ JPR/2015 dated 23.03.2015 passed by the Commissioner (Appeals) confirming service tax demand of Rs.46,92,738/- on banking and other financial services for the period 2005-06 to 2009-10. An equal amount of penalty was also imposed.

2. The appellant is the State Financial Corporation / undertaking of the Government of Rajasthan and has been formed for non-business/ non commercial purposes to facilitate the growth of the industry in Rajasthan. The appellant was registered with the Service Tax Department for providing "Banking and other Financial Services" as

defined in section 65(12) of the Finance Act, 1994¹ and are taxable under section 65(105) (zm) of the Act. During the course of audit of service tax records, the service tax department observed the following:

- (i) The appellant was collecting rent of its immovable property let out for commercial use.
- (ii) The appellant was selling loan application forms, on which no service tax was paid.
- (iii) The appellant was collecting service charges against seed capital assistance sanctioned to the new entrepreneurs.
- (iv) The appellant was collecting financial/foreclosure charges on account of premature repayment of loans by the borrowers.
- (v) The appellant had been collecting financial charges on account of service charges against Working Capital Term Loans.

3. Thereafter, the department issued a show cause notice dated 18.10.2010 for demanding aggregate service tax of Rs.48,51,115/- in respect of above issues and sought to impose penalty under Sections 76, 77 and 78 of the Act. Vide the Order-in-Original No. 113 (ST) JP-I/2012-ADC dated 29.11.2012, the demand was confirmed and equal penalty was imposed. The appellant filed an appeal before the Commissioner (Appeals) who set aside the service tax demand of Rs. 1,58,377/- against renting of immovable property service on the ground that the same had already been confirmed vide an earlier Order-in-Original dated 17.02.2012. Hence, the demand is not liable to be confirmed again for the same period. The remaining service tax demand of Rs. 46,92,738/- was confirmed. The penalties under Sections 76, 77 and 78 of the Act was set aside by extending the benefit of section 80 of the Act with the findings that the appellant is an entity of State Government of Rajasthan and has been formed for non-business/non-commercial purpose. He noted that the appellant had cooperated with the Department and deposited the entire service tax

1 The Act

demand along with the interest before passing the adjudication order. Hence there is no mens rea involved.

4. The appeal against the order of Commissioner (Appeals) was filed on 19.06.2015. The learned counsel appearing for the Appellant presented his arguments on each issue:

(i) **Service Tax on renting of immovable property**

In this regard, the learned counsel informs that the appellant had already deposited the service tax consequent to the adjudication order passed by the Adjudicating Authority. He also submitted that the Commissioner (Appeals) had already dropped the demand of Rs. 1,58,377/- for the period 01.06.2007 to 31.03.2009 which has been accepted by the department. In respect of demand of Rs. 16,117/- for the period 01.04.2009 to 31.08.2009, learned counsel has submitted that the appellant is not pressing this issue.

(ii) **Service Tax on sale of loan application forms**

The learned counsel of the appellant submitted that the sale of loan application forms to the customers is not a service as such and therefore, no service tax is chargeable on sale amount for selling loan application forms. He also pointed out that the person buying loan application form may not necessarily apply for loan., therefore the sale of application form is not a taxable service.

He also drew the attention to Tribunal's order in the case of **Sadhana Educational & People Development Services Pvt. Ltd. Vs. CCE, Pune-III²** wherein it was held that the amount collected on sale of forms, prospectus etc. would not be includible in the value on which service tax is demanded.

(iii) **Service tax of Rs. 3,32,612/- against concessional interest charged under Seed Capital Assistance Scheme**

The learned Counsel submits that the appellant acts as an agent of IDBI, for the implementation of the Seed Capital Scheme of IDBI.

2 2015 (40) STR 1107 (Tri-Mum)

The Scheme is operated by notified State Industrial Development Corporations (SIDCS) and State Financial Corporations (SFCs) as agents of IDBI. The appellant being a State Financial Corporation of the Rajasthan Government helps the new entrepreneurs to start or enlarge their industrial activity through sanctions of seed capital. The main beneficiaries are new entrepreneurs or the small scale industries. Learned Counsel drew the attention of the Bench to Seed Capital Scheme and specifically to paragraph 4 of the scheme which provides that the amount of seed capital assistance per concern shall not exceed 10% of project cost and is subject to ceiling of Rs.15 lacs. As per paragraph 7(i) of the said Scheme, seed capital loan will carry a nominal service charges of 1% per annum for the first five years and interest @10% per annum thereafter. 3/4th of 1% on the amount disbursed by IDBI to the State Financial Corporation for the first five years and thereafter 9.5% per annum was to be deposited with IDBI, as interest. It is well settled principle that interest on loans are not taxable under the 'Banking and other Financial Services' category.

(iv) **Service tax of Rs. 25,30,960/- on foreclosure charges for premature payment of loans**

The learned Counsel submitted that the foreclosure charges are in the nature of liquidated damages to recover the possible loss of interest revenue that would otherwise have been earned by the Banker/Financial Institution in case the loan is repaid as per its normal time frame. The liquidated damages or compensation received by the appellant for foreclosure of loan is not against any service provided by the appellant to the customer and certainly does not fall within the category of "Banking and other Financial Services".

In this regard, the learned Counsel relied on the Larger Bench decision of the CESTAT, Chennai in the case **Commissioner of Service Tax, Chennai Vs. Repco Home Finance Ltd.**³ wherein it has been held that foreclosure charges are nothing but damages which the banks are entitled to receive when the contract is broken by the borrower.

³ 2020(42) GSTL 104 (Tri-LB)

(vi) **Service tax on annual service charges against Working Capital Term Loan**

The learned Counsel informed that the appellant sanctioned loans to the existing borrowers having good track record to meet their working capital requirement without insisting for any fresh security deposit. The appellant charge 1% of outstanding loan as on 31st March every year as service charges. These are not onetime/initial service charges against sanction of working capital loan to the borrower. These charges are in fact additional interest charged from the borrower on the amount of principal loan outstanding at the year end.

5. Learned Authorised Representative stated that the Commissioner (Appeals) has extended the benefit of Section 80 of the Finance Act, 1994. He stated that the Commissioner (Appeals) did not have the power to grant immunity to the appellant from imposition of penalty as the service tax law does not make a distinction between private sector and public sector for liability of interest and penalty.

6. He further argued that the Commissioner (Appeals) had erred in waiving the penalty under the aforesaid sections as the penalty cannot be reduced below the minimum penalty prescribed under Section 76, 77 & 78 of the Finance Act. Since the appellant has not been set up by an Act of Legislature, it cannot be considered a Governmental authority. He relied on the decision of **M/s RIICO LTD Vs. Commissioner of C. Ex., Jaipur-I⁴** The relevant paragraphs are as follows:

"22. However, regarding other services rendered by the appellant to the allottees in the industrial areas, we find no exemption is available. The claim of the appellant that they have undertaken the said maintenance as a Governmental authority and, hence, not liable to tax, is not tenable. The appellant is a corporate company, allotting industrial plots for commercial purpose. As a part of the arrangement of developing industrial areas, they have undertaken certain maintenance works in these industrial areas, which is in furtherance of commercial activity. There is no exemption available for such services prior to 1-4-2014. For the period 1-7-2012 to 30-1-2014 [negative list regime], the appellants claimed that the services rendered are not liable to tax as they are a Governmental authority in terms of Sl. No. 39 of Notification No. 25/2012-S.T., dated 20-6-2012. We note that services by Governmental

4 2018 (10) G.S.T.L. 92 (Tri.- Del).

authorities by way of any activity in relation to any function entrusted to a municipality under Article 243W of the Constitution, is exempted from Service Tax. However, term "Governmental authority" has been defined in the same notification, in para 2(s). For the period prior to 30-1-2014 the appellants are not covered by the definition of "governmental authority" as the same is an authority or any other body set up by an Act of State Legislature. The appellant are not set up by an Act of Legislature. They are a company incorporated by the Government of Rajasthan. However, the services rendered by the appellant after 30-1-2014 are eligible for exemption in terms of Sl. No. 39 of Notification No. 25/2012-S.T., dated 20-6-2012 as the said entry was substituted w.e.f. 30-1-2014, by Notification No. 2/2014-S.T., dated 30-1-2014. The substituted definition changed the scope of "governmental authority" to include any authority or any other body established by Government, with 90% or more participation by way of equity or control, to carry out any function entrusted to municipality under Article 243W of the Constitution. We have perused Article 243W of the Constitution. It empowers Legislature of a State by law endow the municipalities with such powers and authority as has been necessary to enable them to function as institution of Self-Government. The said Article provides for empowering committees to carry out the responsibilities including those listed in 12th Schedule. We have perused letter dated 21-1-2015 of Principal Secretary, Government of Rajasthan, Local Self-Government Department. It is clarified therein that the appellant are carrying out municipal function in their industrial areas as laid down in the Municipal Act, 2009 and the municipal body of the concerned area does not undertake such work in the industrial areas falling under the jurisdiction of the appellant. The matter was further clarified by the Ministry of Finance, Government of India, vide a letter dated 10-1-2017 of Joint Secretary (TRU - II), to the effect that the appellant shall be eligible for exemption from Service Tax in respect of functions entrusted to them in terms of Article 243W of the Constitution w.e.f. 30-1-2014. We note that the 12th Schedule of the Constitution specifies fire services/public amenities including street lightings, parking lights, public convenience etc. as the nature of services to be provided by the municipalities. As such we hold that appellant is liable to Service Tax for the period prior to 30-1-2004 as no exemption is available to them."

Therefore, all the activities/services performed by the appellant are liable to be taxed unless there is implicit remission examination.

7. We have heard Shri S C Kamra & Shri N D Dubey, Advocates appearing for the appellant and Dr. Radhe Tallo, Authorized Representative for the Department.

8. So the issues for consideration before us are as tabulated below:

Sl. No.	Nature of service	Service Tax (including cess) (Rs.) demand	Current appeal status
1.	Renting of immovable property - 01.06.2007 to 31.03.2009	1,58.377	Dropped and accepted by the

			Dept.
2.	Renting of immovable property- 01.04.2009 to 31.08.2009	16,117	This issue is not being agitated by the Appellant
3.	Sale of Loan Application forms	1,13,606	Not accepted, hence agitated
4.	Interest/service charges collected from customers under Seed Capital Loan Scheme.	3,32,612	Not accepted, hence agitated
5.	Service charges for pre-payment / foreclosure of loan account by the customers before the agreed term.	25,30,960	Not accepted, hence agitated
6.	Service charges against Working Capital Term Loans (WCTL) sanctioned to the customers	16,99,443	Not accepted, hence agitated
	Total	Rs.48,51,115/-	Rs.46,92,738/-

9. At the outset, it is important to note that the Rajasthan Financial Corporation has been constituted under a notification of the State Government dated 17 January, 1955 under the State Financial Corporations Act, 1951, for providing long term financial support to tiny, small and medium scale industries in the State of Rajasthan. The Rajasthan Financial Corporation has a network of branch offices wherein all entrepreneurs can approach for loan. The seed capital scheme is operated by the notified State Industrial Development Corporations and the State Financial Corporations as an agent of IDBI. It envisages extension of assistance for meeting the risk capital requirement of entrepreneurs. So all those interested in availing the loan, approach one of the facilitating centers and loan forms is purchased. The appellant also extends Working Capital Term loan to their selected borrowers having good track record.

10. We proceed to discuss each of the issue which are before us:

(i) **Sale of loan forms**: We note that this issue stands decided by the Tribunal vide its order in the case of **Sadhana Educational & People Development Services Pvt. Ltd.** wherein it has held that amount collected for sale of forms prospectus etc. would not be

includible in the taxable value for levy of service tax. For ease of reference, the relevant paragraph is reproduced below:-

“10. We also find that the amount collected towards sale of forms, prospectus will not be includible in the value on which service tax is demanded relying on the Tribunal’s judgment in the case of **Cerebral Learning Solutions P. Ltd.**, 2013 (32) S.T.R. 379 (Tri.-Del.) which held that Notification 12/2003-S.T., dated 20-6-2003 exempts service tax on so much of the value of taxable service as is equal to the value of the goods and materials sold by the service provider to the respondent of service. The same decision was taken by the Tribunal in the case of **Chate Coaching Classes P. Ltd.**, 2013 (29) S.T.R. 138.”

10.1 We also note that the Tribunal held the same view in its decision in the case of **Cerebral Learning Solutions Pvt Ltd vs. Commissioner of Central Excise & Service Tax, Indore**⁵ which was upheld by the Supreme Court in the appeal filed by the Department viz., **Commissioner of Central Excise & Service Tax, Indore vs. Cerebral Learning Solutions Pvt Ltd.**⁶ Accordingly, we hold that the sale of loan application forms is not a taxable service and therefore, no demand is leviable on such sale of loan forms.

(ii) **Seed Capital Assistance Scheme:** We have carefully gone through Seed Capital Loan Scheme document. Paragraph 7 under heading terms and conditions of the assistance, states the following:

“(i) Rate of Interest

The seed capital (soft loan) will carry a nominal service charge at 1% per annum for the first five years and interest at 10% per annum thereafter. IDBI would levy service charge of three-fourth of 1% on the amount disbursed to SDICs/ SFCs from the date of disbursement for the first 5 years and 9.5% per annum thereafter.”

From the above, it is amply clear that though the term used in ‘service charge’ but the underlying nature of the 1% and 10% is nothing but interest on the seed capital loan, extended to the entrepreneurs. Therefore the same is not liable to service tax. As observed, it is a

⁵ 2018(10) G.S.T.L. 37 (Tri.-Del.)
⁶ 2022 (1) Centax 7 (S.C.)

settled principle of law that interest on loans is not taxable to service tax.

(iii) Service tax on the service charge for prepayment/foreclosure of premature payment of loan:

We note that the leviability of Service Tax on foreclosure has been examined in detail by this Tribunal in **Repco Home Finance Ltd.**⁷ The relevant paragraphs are extracted below:

"21. It is, thus, clear that where service tax is chargeable on any taxable service with reference to its value, then such value shall be determined in the manner provided for in (i), (ii) or (iii) of sub-section (1) of Section 67. What needs to be noted is that each of these refer to "where the provision of service is for a consideration", whether it be in the form of money, or not wholly or partly consisting of money, or where it is not ascertainable. In either of the cases, there has to be a "consideration" for the provision of such service. Explanation to sub-section (1) of Section 67 defines "consideration" to include any amount that is payable for the taxable services provided or to be provided, or any reimbursable expenditure, or any amount retained by the lottery distributor or selling agent. It is clear from the aforesaid definition of "consideration" that only an amount that is payable for the taxable service will be considered as "consideration". This apart, what is important to note is that the term "consideration" is couched in an "inclusive" definition.

22. A Larger Bench of the Tribunal in *Bhayana Builders (P) Ltd. v. Commissioner of Service Tax* [2013 (32) S.T.R. 49 (Tri. - LB)] observed that "implicit in the legal architecture is the concept that any consideration whether monetary or otherwise, should have flown or should flow from the service recipient to the service provider and should accrue to the benefit of the latter." In the said decision, the Larger Bench made reference to the concept of "consideration", as was expounded in the decision pertaining to Australian GST Rules, wherein a categorical distinction was made between "conditions" to a contract and "consideration". It has been prescribed under the said GST Rules that certain "conditions" contained in the contract cannot be seen in the light of "consideration" for the contract and merely because the service recipient has to fulfil such conditions would not mean that this value would form part of the value of the taxable services that are provided.

23. The Supreme Court in *Commissioner of Service Tax v. M/s. Bhayana Builders* [2018 (2) TMI 1325 = 2018 (10) G.S.T.L. 118 (S.C.)], while deciding the appeal filed by the Department against the aforesaid decision of the Tribunal, also explained the scope of Section 67 of the Act, both before and after the amendment, in the following words :

"The amount charged should be for "for such service provided" : Section 67 clearly indicates that the gross amount charged by the service provider has to be for the service provided. Therefore, it is not any amount charged which can become the basis of value on which service tax

becomes payable but the amount charged has to be necessarily a consideration for the service provided which is taxable under the Act. By using the words "for such service provided" the Act has provided for a nexus between the amount charged and the service provided. *Therefore, any amount charged which has no nexus with the taxable service and is not a consideration for the service provided does not become part of the value which is taxable under Section 67.* The cost of free supply goods provided by the service recipient to the service provider is neither an amount "charged" by the service provider nor can it be regarded as a consideration for the service provided by the service provider. In fact, it has no nexus whatsoever with the taxable services for which value is sought to be determined."

(emphasis supplied)

27. What follows from the aforesaid decisions is that "consideration" must flow from the service recipient to the service provider and should accrue to the benefit of the service provider and that the amount charged has necessarily to be a consideration for the taxable service provided under the Act. It should also be remembered that there is marked distinction between "conditions to a contract" and "considerations for the contract". A service recipient may be required to fulfil certain conditions contained in the contract but that would not necessarily mean that this value would form part of the value of taxable services that are provided.

35. The "expectation interest" is a popular measure for damages arising out of breach of contract. The foreclosure charges, therefore, are not a consideration for performance of lending services but are imposed as a condition of the contract to compensate for the loss of "expectations interest" when the loan agreement is terminated prematurely. In fact, foreclosure charges seek to deter the borrowers from switching over to cheaper available sources of loan, as has been so clearly stated in the Circular dated 26 June, 2012 issued by the Reserve Bank of India.

36. The basis for charging foreclosure amount has also been explained by the Karnataka High Court in *M/s. Hotel Vrinda Prakash and Another v. KSFC and Another* [ILR 2008 KAR 1311]. The writ petitioner had borrowed a loan from the Karnataka State Financial Corporation but before the period of loan could expire made an application for foreclosure of the loan. The Corporation, however, demanded premium on the advance payment/foreclosure amount which demand was challenged in the writ petition. The High Court, after noticing that the contract contained a clause giving discretion to the Corporation to impose premium on the balance amount of loan, observed that granting of loans is a business of the Corporation and if the loan is prepaid, the Corporation may have to suffer loss. It is to overcome this situation that premium is charged. The observations are as follows;

"13.....Therefore, the granting of loans or advances is one of the business of the Corporation. As stated above, the Corporation borrows funds from the financial institution at the prevailing rate of interest. If an account is prepaid/foreclosure when the interest rates are falling, the Corporation may have to suffer loss. To overcome this situation, if a premium is charged on the outstanding loan being

prepaid, the same cannot be found fault with. I am of the considered view that the Corporation has the power and authority to levy prepayment/foreclosure premium.”

37. The foreclosure of loan is, therefore, a material breach of contract as it curtails the loan service period unilaterally, which can prompt the promisor to claim damages. Damages can be determined by Courts or they can also be incorporated in the loan agreements and other commercial contracts so as to ensure certainty in dealings and also serve as a deterrent measure. This aspect of damage is known as liquidated damages.

54. The reference is, accordingly, answered in the following terms:

“Foreclosure charges collected by the banks and non-banking financial companies on premature termination of loans are not leviable to service tax under “banking and other financial services” as defined under Section 65(12) of the Finance Act.”

(emphasis supplied)

In view of the above decision, we hold that the service charges for pre-payment or foreclosure of loan amount by the customer cannot be treated as taxable service and is not chargeable to service tax.

(iv) Service charge against Working Capital Term Loan: A perusal of the scheme for short term financing of Working Capital Term loan reveals that the scheme was meant for all small scale and medium scale industrial units financed by the Corporation. Para 7 of the scheme document discloses that the interest liable on such Working Capital Term loan. Paragraph 12 illustrates the Service Charge payable on such loans. The said paragraphs are reproduced for ease of reference:

“7. Rate of Interest: The interest on working capital term loan shall the same what is chargeable on term loan to Small Scale Industries and medium scale units at the time of execution of documents:-

12. Service charges: The borrower shall pay service charges yearly @ 1% per annum payable quarterly on the outstanding amount for Working Capital Term loan. The first payment shall

fall due after the expiry of one quarter on the date as 1st April/ 1st July, 1st October or 1st January.”

11. Learned Counsel has argued that though the heading indicated is Service Charge, the 1% charge is actually akin to the interest charged on the Working Capital Term loan. We are unable to accept this argument of the learned Counsel. The scheme document has clearly differentiated between the interest liable to be charged on such loans and the service charges on such loan. Therefore service charges of 1% indicated separately clearly shows that this amount is a consideration for the services being provided by the appellant to the borrowers. It is apparent that the said service charge is a financial charge on account of providing financial services of loans and advances. In view of the same, we hold that service tax is leviable on the service charge, realized on Working Capital Term Loan by the appellant.

12. We note that the learned Authorised Representative has argued that the Commissioner(Appeals) has erred in waiving the penalty under Section 76, 77 & 78 of the Act. The Appellant is a State Government enterprise, and in such a case allegation of willful suppression of facts with an intention to evade the duty payment cannot be made. It is seen that the Tribunal in several cases has held that where the waiver of penalty under Section 80 of the Act is based on the bona fide belief on the part of the appellant that the extended period would not be invokable in as much as the same ingredients are required for invocation of extended period of limitation. It is pertinent to point out that other issues raised by the Department are already settled to be not taxable. Hence, there was certainly a bonafide belief of the Appellant that no service tax was leviable on the financial services provided by them. In view of the above, we hold that the waiver of penalty under section 80 of the Act has been correctly invoked by the Commissioner (Appeals).

13. In view of the above discussions, we uphold the demand of Rs. 16,99,443/- with applicable interest. The remaining demand is set aside. The Order-in-Appeal stands modified accordingly.

(Pronounced in the open court on 13 .03. 2023)

(JUSTICE DILIP GUPTA)
PRESIDENT

(HEMAMBIKA R. PRIYA)
MEMBER (TECHNICAL)

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