

SHM Insights Indirect Taxation

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Supreme Court Dismisses Civil Appeal Against CESTAT Ruling on Intermediary Definition holding that services rendered on a principal-to-principal basis will not be covered under the definition of intermediary



Summary

This tax alert summarizes the recent decision by the Hon'ble Supreme Court of India pertaining to the rejection of a civil appeal¹ originating from the Customs Excise and Service Tax Appellate Tribunal ('CESTAT'). The CESTAT had previously concluded that the provision of incidental services, such as vendor selection or goods production by those vendors, incidental to the primary supply or procurement of goods carried out on a principal-to-principal basis, does not meet the criteria for classification as intermediary services under the ambit of service tax. The Hon'ble Supreme Court of India has upheld this stance by dismissing the appeal, thereby affirming the CESTAT's ruling². The ruling clarifies that compensation received cannot be subjected to taxation as intermediary services in scenarios where an Assessee facilitates orders from foreign buyers for the export of goods from Indian exporters and provides a range of services to such foreign buyers on a principal-to-principal basis.

Brief Background

1. Issue is regarding services rendered by the taxpayer during the period October 2014 and March 2016;
2. The taxpayer was involved in the acquisition of garment supply orders from overseas buyers. Subsequently, it instructed the Indian sellers or manufacturers to dispatch garments to international buyers and received compensation in foreign currency via banking channels.
3. The taxpayer raised the invoice for support services rendered in relation to the procurement of goods for export and received commission to procure various orders from buyers for export to a foreign country. The commission amount was computed as a percentage of the Free on Board ('FOB') value of the exported goods.
4. The taxpayer provides array of services encompassing product design and development, vendor evaluation and enhancement, quality assurance, inclusive of live production sample testing, logistical and operational facilitation for vendors.
5. The Department issued a show cause notice to the taxpayer demanding service tax on such

commission earned, holding that the services provided by the taxpayer were covered under the definition of intermediary services as per Rule 2(f) read with Rule 9(c) of the Place of Provision of Services Rules, 2012. The show cause notice was subsequently adjudicated.

6. Discontented with the original adjudication, the Assessee pursued an appeal before the Tribunal, Chennai Bench. The Tribunal ruled in favor of the Assessee.
7. Aggrieved by the order of the Tribunal, the revenue filed an appeal before the Hon'ble Supreme Court which dismissed the appeal on merits.

Taxpayer's assertions before the CESTAT

The impugned activity would not fall within the ambit of the definition of 'intermediary service' as Assessee had rendered a bouquet of services including procurement of goods, selection of vendors, monitoring the quality of goods, designing and live testing of samples and carrying out various other quality checks till the final dispatch to the foreign buyer) to the foreign buyer on a principal-to-principal basis. Since, the activity is on a principal-to-principal basis, the activity of promotion of products and solicitation of orders is an export of services.

Revenue's assertions before the CESTAT

- The impugned activity of the Assessee would be covered under the definition of 'intermediary services' since the Assessee facilitates the provision of supply of goods between two persons. Taxpayer could not amend the value of goods supplied, the consideration i.e. commission is identifiable from the value of exported goods; and, as per the agreement with the buyer, Assessee is authorised to act on behalf of the foreign buyer. Hence, the services are for procurement of goods.
- The expression 'arranges or facilitates' in the definition of 'intermediary' would cover within its ambit a host of marketing and sales promotion activities that are provided in relation to the arrangement and/or facilitation of a main service/supply of goods. Thus, the services are not provided on a principal-to-principal basis.
- Further, the impugned activity does not fall under the excluded categories of intermediary i.e., person who provides the main service or supplies the goods on his account and therefore, the services rendered by the Assessee do not qualify as 'export of service' since the condition of Rule 6A of the Service Tax Rules, 1994 i.e., 'the place of provision of service should be outside India' is not fulfilled.

CESTAT Ruling

The principal issue brought before CESTAT pertained to the classification of the taxpayer's services within the category of intermediaries. In a previous ruling concerning the same taxpayer, CESTAT meticulously examined the parameters defining an intermediary, elucidating several crucial points:

- The taxpayer's services are furnished on a principal-to-principal basis, strictly in accordance with the directives issued by its foreign clients.

- A comprehensive array of services, including but not limited to procurement facilitation, vendor selection, quality oversight, sample design, live testing, and various quality assessments until the final dispatch of garments to foreign clients, underscores the taxpayer's multifaceted role, extending beyond mere transactions.
- Vendor selection, being an incidental service in the procurement process, is executed in accordance with the specifications and guidance provided by the foreign clientele.
- The remuneration received by the taxpayer, computed based on the free-on-board value of garment exports, does not implicate the taxpayer as an intermediary.

Consequently, CESTAT determined that the taxpayer's services do not fall within the purview of intermediary activities, thereby overturning the demand order confirming the imposition of service tax.

Apex Court's decision and confirmation

The Hon'ble Supreme Court of India dismissed the appeal of the Revenue. It held that Assessee does not fall within the scope and ambit of the definition of 'intermediary'.

Key takeaways from the Ruling

The Apex Court's validation of the CESTAT's order marks a significant development, particularly given the widespread challenges in defining the role of intermediaries due to the absence of statutory precision. This endorsement, particularly from the highest judicial authority, is poised to significantly reduce litigation surrounding similar issues.

Moreover, the similarity between the definition of intermediary in the service-tax and Goods and Services Tax ('GST') regimes suggests that the jurisprudence stemming from this decision could offer valuable guidance to taxpayers affected under the GST framework. However, it may be noted that there is no exposition of law on intermediary issue by the Apex Court itself and hence it cannot be said that in light of this ruling, the controversy stands resolved altogether. Further, as the issue is highly fact specific, the same needs to be tested on the basis of relevant facts and applicable provisions.

¹ Civil Appeal No. 8343/2024

² Service-tax Appeal No. 41459 of 2019

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