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Court : Customs Excise and Service Tax Appellate Tribunal CESTAT Ahmedabad

Decided On : Jun-06-2007

Reported in : (2007)10STJ227CESTATAhmedabad

Judge : M Ravindran, V T M.

Appellant : Foster Wheeler Energy Ltd.

Respondent : Cce and C

Judgement :

1. This is an appeal against the order of Commissioner (Appeals) No.dt.28/3/2004, by which the order of original authority dt.29/3/2004 has been upheld.2. Heard both sides. The Ld. Advocate for the appellants also filed a written submission dt. 18/5/2007.

a. M/s. Petronet LNG Ltd. (PLL) was engaged in the business of setting up and operating LNG terminal for receiving, storage, de-gasification facility at Dahej, Gujrat. For the said purpose, PLL entered into two contracts which are mentioned below.

b. PLL entered into an EPC contract with M/s. Ishikawajima-Harima Heavy Industries Ltd., Japan to develop, design, engineer and procure equipment, materials and supplies, to erect and construct storage tanks of 5 MMTPA capacity, with potential expansion to 10 MMTPA capacity at the specified temperatures. The EPC contract also envisaged providing marine facility (jetty and island brake

water) for transmission and supply of LNG to purchasers. The project involved, inter alia, offshore supply, offshore services, onshore supply, onshore services and construction & erection.

c. PLL entered into an agreement dt. 15/1/2001 with the appellant for project management consultancy in relation to setting up and operating the above said LNG terminal.(This agreement is directly relevant for the present proceedings.) d. The agreement detailed the various areas in which the appellant was required to advise, assist in relation to the execution of the project.

e. The agreement contemplated the provisions of both offshore services and onshore services. For the said purpose, the agreement also defined the terms like onshore services and offshore services.

The rates specified are different for offshore services and onshore services.

f. PLL settled the amounts as per the invoices issued by the appellants after making a verification of the particulars.

g. The original authority held that the services rendered by the appellant to PLL came under the category of consulting engineers.

Accordingly, he confirmed a sum of Rs. 1,03,73,013/- as service tax along with interest on the fee collected amounting to Rs. 21,65,63,780/- on onshore services relating to the period Jan. 2001 to April, 2003. Similarly, he confirmed a sum of Rs. 48,05,821/- as service tax along with interest towards offshore services rendered by them on the total fee collected amounting to Rs. 10,05,40,183/- relating to the period. In addition a penalty of Rs. 500/- under Section 75A and a penalty of Rs. 1000/- under Section 77 were imposed. Further under Section 76, a penalty of Rs. 200/- every day during period of default from 26/6/2001 until the service tax is fully paid was imposed. Further a penalty of Rs. 2 crores under Section 78 was also imposed.

4.1. Ld. Advocate appearing for the appellant took us through the various clauses contained in the project management consultancy agreement dt. 15/1/2001. In particular, he drew our attention to the definition relating to home places, onshore

services/offshore services.

He took us through Clause No. 313 which relates to the locations for performing the services by the appellant. He took us through the provisions relating to the fees payable which is partly a fixed component and a variable component in respect of both onshore services and offshore services as provided in Sub-clause 7.1; He also took us through the scope of services provided by the appellant in the light of said agreement.

4.2. He submits that the services rendered by the appellant is not limited to the field of engineering. The appellant is not stopping with the rendering advice, but actively involved in monitoring implementation and in trouble shooting; they cannot be treated as rendering 'consultancy engineering services'; further services rendered by them cannot be treated as merely in the field of engineering and therefore, the contract should not be vivisected to hold that part of the services are to be treated as consulting engineering services.

4.3. He submits that the project management services provided under the agreement are not the services of consulting engineer as defined in Section 65(13) of the Finance Act, 1994. In order to attract service tax under the category of consulting engineer, the service must be in the nature of advice, consultancy or technical assistance and the same should be in the discipline of engineering. However, in the present case, the Appellants provided the services which was the combination of engineering, administration and financial services. As per Clause 2.2 of the agreement, the Appellants were to provide the all services as specified in the agreement and the Appellants were paid the single consideration for providing the all services in agreement.

4.4. He submits that the entire transaction has to be seen as a whole and one part of the transaction cannot be seen in isolation for purpose of taxation. By treating the agreement as a single contract, it is clear that the Appellants provided the services which are the combination of engineering, administration and financial services for a single consideration. The services provided under the agreement are not solely in the discipline of engineering. Further, the services are not purely in cerebral nature. Hence the appellants are not liable to pay service tax on the

consideration received under the agreement. In this regard, the appellants place reliance on the case of Daelim Industries Ltd. 2003(155) ELT 457 (affirmed by SC reported in 2004 (170) ELT A181) wherein it has been held that the contract cannot be vivisected for purpose of taxing a part of the contract.

4.5. The appellants have their permanent establishment in United Kingdom and the appellants have no registered office in India. Hence the appellants are not liable to pay service tax. Though the appellants have the project office in India, the said office cannot be treated as office of the service provider for the purpose of service tax.

4.6. Section 64 of the Act clearly provides that the Act applies to the services rendered in India except in the State of Jammu & Kashmir. The services rendered outside India are not covered under the ambit of service tax. The said position was also clarified by the CBEC vide circular No. 36/4/2001 dt. 8/10/2001.

4.7. The terms of the agreement between PLL and Ishikawajima-Harima Heavy Industries Ltd. came for scrutiny by the Hon'ble Supreme Court reported in 2007 TIOL 03-SC-IT. Hon'ble Supreme Court has held that the Indian Taxing Authority has no right to tax the transaction undertaken outside India. The Hon'ble Supreme Court held that even though the contract is turnkey contract and cannot be vivisected, however, where the question of jurisdiction is involved, the entire transaction cannot be taxed by treating the agreement as a single contract. The Supreme Court therefore held that the services undertaken outside India though used in India cannot be taxed by the Indian Taxing Authorities.

Ishiwajama-Harima Heavy Industries Ltd. is one of the contractors who executed the construction of re-gasification terminal of PLL. The appellants submit that the above said judgment squarely covers the offshore services provided by the appellants under the agreement.

Hence, the amount charged for providing the offshore services will not be liable to service tax.

4.8. It is further submitted that the services rendered outside India are made liable to service tax in view of Section 66A which has been inserted in the service tax provisions by the Finance Act, 2006 with effect from 18/4/2006. Therefore, prior to this date, services rendered outside India are not taxable under the provisions of Finance Act, 1994.

4.9. The appellants submit that the services provided under the agreement are not liable to service tax under 'consulting engineer'.

Further the appellants are non-resident and do not have any registered office in India, hence the appellants cannot be made liable to pay service tax. In any case, the services provided outside India are outside the coverage of service tax authorities. The appellants therefore submit that they were and still are of the bonafide view that they are no liable to pay service tax. The appellants did not have any intention to evade the payment of service tax. In fact, the appellants have deposited the service tax along with interest prior to issue of the SCN in respect of onshore services. Hence, no penalty can be imposed on the appellants.

5. The Id. DR also took us through various provisions of the agreement and submitted that they are rendering services because of extensive experience in the field of engineering. Their role is that of consultancy advisory management services. The agreement specifies the qualification of personnel to be employed by the appellant for the purpose of rendering such consultancy, advise of PLL. The minimum qualification prescribed is a degree in engineering and in many cases, experience in specialized fields of engineering is a must. The Clause 2.2 provides the technical specifications, Clause 4.1 prescribes the master production schedule, goes to explain the man power requirement, and Clause 4.3 explains the activity schedule, the Clause 5.1 stipulates that sub-contract of work assigned to the appellant is not permissible except by approved associate co. with the engineering expertise in relation to marine engineering. The services provided by the appellant is in the nature of advice, consultancy in areas relating to selection of man power by EPC contractor, selection of material, selection of technical specification of various contractors, and all these are possible only with the engineering expertise as prescribed in the agreement. Therefore, the appellants

are basically and predominantly rendering engineering consultancy services in specified fields.

6.1. We have carefully considered the submissions of both parties. A careful reading of the agreement between the appellant and PLL indicates that the appellant is not in actual execution of the project.

The project management functions relating to the project continued to be with PLL. The execution of the project is undertaken by a consortium of EPC contractors led by M/s. Ishikawajima-Harima Heavy Industries Ltd.. The appellant is in the role of adviser/ consultant to PLL, so that the work of the EPC contractors are as per the requirements and standard envisaged by PLL.

6.2. The work of the EPC contractors is undoubtedly in the field of engineering. It is a highly specialized work and requires to develop, design, engineer and procure equipment materials and supplies, to erect and construct the LNG terminal.

6.3. The appellant has been engaged by the PLL in getting advice / consultancy in relation to the above specialized work undertaken by the EPC contractors. They have been chosen admittedly because of the extensive experience in the area of design and engineering and related activities. Without that, the question of their apprising and advising on the quality of material, the quality of technical manpower employed, the quality of work undertaken by the EPC contractors cannot arise.

6.4. The agreement elaborately mentions category of managers, engineers and other technical personnel, who are to form a team in rendering the work in pursuance of the agreement dt. 15/1/2001. They envisage minimum qualification for every person, a bachelor's degree in engineering. It also envisages in many cases long years of experience in major engineering projects. In some cases also envisages qualification in business administration. In whatever field, when the people rise high in the organization, management expertise becomes a necessity. Whether they can be treated as engineers with management expertise or managers with engineering expertise 6.5. Rendering advice on choice of materials, looks as if it is mainly on a commercial aspect. Considering the sophisticated nature of the engineering project, the expertise required is more

about the technical specifications and requirements of the materials and the commercial aspect appears to be not the main issue but a secondary issue.

Similarly rendering advice in selection of personnel looks to be an exercise of HR Department. The choice of personnel for the sophisticated project of this nature depends more on the assessment of the technical skill of the personnel chosen and the other skills required appear to be of secondary importance. In assessing the quality of work executed by the specialized engineers of the EPC contractors also, the emphasis is on the technical knowledge of the consultants and engineers.

6.6. The above aspects are clearly brought out from a close reading of the agreement dt. 15/1/2001, which both the appellant and the department have relied upon. The reports sought to be submitted, the records sought to be maintained are all of technical nature and therefore there is no doubt in our mind that the services rendered is essentially, pre-dominantly in the field of engineering. Therefore, the Commissioner's findings that the appellant is rendering the services of consulting engineer is well founded.

6.7. The appellant have submitted that part of the services are rendered from outside India. The agreement entered into by them clearly indicates that certain service are rendered outside India and the detailed billing agreed upon between the appellant and PLL based on man days spent separately for onshore and offshore services confirms this.

The very same agreement is being relied upon to conclude that the assesseees are rendering the services of consulting engineers and the said agreement also clearly specifies which are onshore services and which are offshore services. It also indicates the rates for off-shore services are higher. PLL was not expected to pay a much higher amount by classifying the on-shore services as off-shore services, just to avoid some percentage as service tax.

6.8. We also noticed that there has been an amendment by way of inserting Section 66A in the Service Tax Provisions by the Finance Act, 2006 w.e.f. 18/4/2006. There is no doubt that the services rendered are ultimately in relation to

setting up of the LNG terminal in India.

Nevertheless, no reliable evidence has been adduced to contradict the claim of the appellant that the services claimed by them as off-shore services are not offshore services. Such offshore services are liable for tax consequent to the amendment w.e.f. 18/4/2006, but for earlier period the same will not be so.

6.9. Service Tax circular No. 36/4/01 dt. 8/10/2001 holds that service provided beyond the territorial waters will not attract service tax.

This circular will be relevant till the amendment brought out in service tax laws by insertion of Section 66A w.e.f. 18/4/2006.

Therefore, the appellant's contention that the demand on services relating to identified offshore services cannot be subjected to service tax during the relevant period is acceptable.

7. The appellant have made a submission that the quantum of service tax on the on-shore services should be restricted to Rs. 88,18,761/- instead of Rs. 1,03,73,013/- as the Commissioner (Appeals) has taken the entire amount realized as taxable value instead of treating them as cum- duty value; the service charges have been calculated as having been realized at an average exchange rate of Rs. 48.50/- per US\$ even though in several cases they have received at conversion rates which are lower than Rs. 48.50/- per US\$; certain amounts billed but not received has already been taken into account for calculating the service charges. Their submissions have not been contested by the Ld.

DR. These submissions are therefore relevant and acceptable. Therefore, the actual duty liability is restricted to Rs. 88,18,761/- as claimed by the appellant.

8. Regarding imposition of penalty, it is noticed that the appellant not only shown the service tax separately on the invoices but also recovered the amount from PLL. There was no justification on the part of the appellant to collect the service tax from PLL through the invoices and not to pay the service tax. Under these circumstances, the claim that they were not having any intention to evade service tax and they were under a mistaken impression that service tax was not payable is

not acceptable. Therefore, the findings of the Commissioner (Appeals) that there was suppression of facts with intention to evade service tax is legally sustainable.

a. The appellant has been rendering the services of consulting engineers to PLL. The services rendered by them under the category of on-shore services are liable to service tax and the services under the category of off-shore services are not taxable for the period prior to 18/4/2006.

b. The service tax payable should be determined on the actual amount received adopting the total realization as gross amount.

c. The appellant is liable for penalty inasmuch as they have suppressed relevant details and failed to pay the service tax even after collecting the same from PLL.

a. The demand of service tax is restricted to Rs. 88,18,761/- towards on-shore services rendered by the appellant. The interest applicable on the above amount shall be payable in terms of Section 75 of Chapter-V of the Finance Act, 1994.

b. The demand of Rs. 48,05,821/- as service tax towards offshore services is set aside. Consequently the interest demanded relating to the demand of service tax is also set aside.

c. The penalty imposed under Section 78 is reduced to Rs. 22,04,690/-

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