

Draft Circular on Refunds in Service Tax

(This is a draft Circular proposed to be issued in order to streamline the process of sanctioning of refund claims, mainly arising on account of service tax borne on input services that have gone into exports of services in terms of notification no. 5/2006. This draft is being placed in public domain for widest possible circulation and an extensive debate from all stakeholders in trade and industry as also from all the field formations of the department. All suggestions and feedback may please be emailed at d.aron@nic.in to Shri Deepankar Aron, Director (Service Tax), CBEC (Phone No. 011-23092747 and Fax No. 011-23092275) by 30th November 2011. The feedback and suggestions received would be considered for revising the draft circular.)

Draft Circular No. _____ / _____ /2011 – Service Tax

Subject: Problems faced by exporters in availing refund of excess credit – regarding

Representations have been received both from the field and the trade regarding difficulties being faced in the determination of the input services which are eligible for refund under notification 05/2006. Resultantly, the issue has spawned delays and disputes, which has necessitated the issue of this clarification.

2. The issue of eligibility of input services to refund under notification no. 05/2006 has been addressed in Circular No. 120/01/2010-ST dated 19th January, 2010 in paragraph 3.1. The criterion laid down in this paragraph for determining the eligibility states that “in case the absence of such input/input service adversely impacts the quality and efficiency of the provision of service exported, it should be considered as eligible input or input service”. This criterion has not been very useful as it is found to be too conceptual and not easily translatable into objective tests that could help in deciding actual cases. Thus a need has been felt for further elaboration by the Board on this issue.

3. The objective that is sought to be achieved by the refund of cenvat credit under notification 05/2006 is to zero-rate the exports. Zero-rating means that the goods and services that are exported from the country should not be burdened with any excise or service taxation. For a 100% exporter who has no domestic business this can be realized only when the ambit of services that are covered by

notification 05/2006 is congruent with the ambit of services that are covered by the definition of “input service” that is given in Cenvat Credit Rules, 2004. Thus every input service has to be eligible for refund under notification 05/2006 for a 100% exporter who has no domestic business.

4. The above clearly implies that the scope of Rule 2(l) is congruent with the scope of Rule 5 and the scope of both is congruent with the scope of Notification No. 05/2006 i.e. any service that satisfies the definition of input service as given in Rule 2(l) would also fall within the mischief of Rule 5 and also of Notification No. 05/2006. This is necessary for a perfect pass through from Rule 2 (l) to Rule 5 to Notification No. 05/2010. Only such a construction can zero-rate the exports.

5. For a business entity that has both export business and domestic business the only additional requirement is to check whether the input service has contributed exclusively to domestic business. If the input service has made no contribution to exports and has been exclusively utilized for domestic operations the service has clearly not contributed to exports and so would not be eligible to refund. For example an advertising campaign for a product that is sold exclusively in the domestic market would not contribute to exports and so would not be eligible for the benefit of notification 05/2006. Every input service that is not identifiable as contributing exclusively to domestic business can be said to have a link with exports though its contribution to export may vary. In order to extract the extent of contribution that the input service has made to exports, notification 05/2006 provides for multiplying the credit that has been taken on an input service with the correction factor (export turnover/ total turnover). It is this extracted amount which indicates the contribution that the input service has made to exports. The extracted amount is also the maximum possible amount that is eligible as refund as per the current statute. In this backdrop, it would not be necessary to link every input service invoice with an output invoice, so long as the input service has a link with the export as discussed above.

6. Field formations and trade have represented about the problems being faced in identifying and linking the input services that have gone into providing the output services. Accordingly, the method to be followed for determining eligibility to refund can be summed up in the following principles:

(1) Check that the service on which refund is claimed satisfies the definition of input service that is given in Rule 2 (1) of the CENVAT Credit Rules, 2004.

(2) Next, service is eligible to refund unless facts of the case indicate that the benefit of the service has gone exclusively into domestic business with no spill over what-so-ever into export business.

(3) The second principle mentioned at sub-para (2) above is to be given a strict construction. Disqualification on this account would be an exception rather than a rule and should be done only when there is unmistakable indication that the benefit of the service has not gone into export business what-so-ever.

(4) The level at which a determination shall be made of whether the input service has gone exclusively into domestic business or not shall be at the level of the 'input service invoice'. The officer scrutinizing the claim will not disaggregate the invoice and extract elements from it and state that these elements have exclusively contributed to domestic business. If at the level of aggregation that is reflected in an invoice, a portion of the input service that is embodied in the invoice has contributed to exports, then the entire input service invoice shall be eligible for refund.

7. Keeping the above principles and statutory provisions in mind, as also after considering the feedback from the field formations on eligibility of input services, a list of input services that are eligible for grant of refund has been prepared and is in the Annexure. Apart from the conditions mentioned above, certain other conditions subject to which the refund would be applicable are also indicated therein. It may please be noted that the list is not exhaustive, but is illustrative. Further, the exact application would depend upon the facts of each case.

8. It is expected that the principle that has been outlined above would prove useful in determining eligibility to refund of the input services. At the same time, it is expected that the field formations shall strengthen the audit machinery including the pre-audit and the post audit mechanisms, so as to ensure that the process of sanctioning of refund is taking place in due accordance with the statutory provisions, so as to prevent the possibility of any misuse.

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9. It is hoped that with the issuing of this circular, smooth and expeditious disposal of exporters claims for refund shall follow. In case of any doubt, an immediate reference may be made to the Board.

Yours faithfully,

(Deepankar Aron)
Director (Service Tax)

Annexure**List of Services on which refund is allowed (fully or partially)**

S. No.	Category of Service	Exclusions or Limitations, if any	Remarks
1	Advertising agency's services 65(105)(e)		A company hires advertising agency for programming, broadcasting and releasing activities related to advertisements. This promotes the brand of the company which enhances its sales and hence is directly related to provision of output service.
2	Air travel agents services 65(105)(i)	Should not be allowed in case it is for personal use of employees	The services are procured by a company in relation to travel of employees for conducting business meeting and attending seminars towards professional objectives. Hence it is an eligible input service for exporting the taxable output service. These services are required for travel and tour of their employees in relation to the company's business which are essential for maintain orders and efficient work of the business i.e. export of services.
3	Asset management service 65(105)(zzzzc)	Should not be allowed in case for personal use of employees.	May be allowed when used for Banking and other financial services.
4	Banking and other financial services 65(105)(zm) & (zzk)	Should not be allowed in case for personal use of employees.	These input services are required for issuance of bank guarantee for overseas project / other business activities.
5.	Business auxiliary services 65(105)(zzb)		These input services are required for procurement of orders and some similar activities.
6.	Business exhibition services 65(105)(zzo)		These services would be required for furtherance of business activities.
7.	Business support		Accounting payroll, transaction

	services 65(105)(zzzq)		processing, routine administration, customer relationship management, telemarketing and IT support services are taken by the company to maintain the day to day operations of the company and are very much the input services on which refund would be eligible.
8.	Cargo handling service 65(105)(zr)		Should be allowed as it is used for business purposes.
9.	Chartered accountant's services 65(105)(s)	Should not be allowed in case for personal use of employees.	These services are required not only for maintaining the accounts and auditing the records but also for complying with the statutory requirements. Hence, these input services are essential for the business of export of services. Further, these services help to strengthen the internal controls for smooth functioning of the business.
10	Cleaning activity service 65(105)(zzzd)	Should not be allowed in case for personal use of employees.	Cleaning activities of the office premises are necessary to enable the employees of the company to perform efficiently.
11	Clearing and forwarding agent's services 65(105)(j)		Should be allowed as it is used for business purposes.
12	Commercial training or coaching service 65(105)(zzc)	Should not be allowed in case for personal use of employees.	These services are procured by a company so that employees can get regular updates of various changes in laws and technology during seminars, coaching or trainings.
13	Company Secretary Service 65(105)(u)		These services are required for complying with the requirements of Companies Act, 1956 as the assesses are normally registered under the said Act.
14	Consulting engineer's services 65(105)(g)		Various engineers are consulted for providing advice in respect of the output service and the same is used in relation to export.

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15	Convention services 65(105)(zc)	Should not be allowed in case services are procured as a staff welfare measure.	As per Circular 120/01/2010-ST dated 19 January 2010, it should not be allowed for entertainment or staff welfare, however for official purposes, these are very much valid input services.
16	Copyright services 65(105)(zzzt)	Should not be allowed in case for personal use of employees	Should be allowed as these are used for professional activities.
17	Cost accountant's services 65(105)(t)	Should not be allowed in case for personal use of employees	Should be allowed as these are used for professional activities.
18	Courier service 65(105)(f)	Should not be allowed in case for personal use of employees.	These services are consumed by a Company for delivery of business documents. The delivery of these documents is essential to process transactions related to exports. Hence, a valid service.
19	Credit rating agencies 65(105)(x)		These services are used for professional purposes.
20	Custom house agent's services 65(105)(h)		These services are used for professional purposes in relation to exports.
21	Design services 65(105)(zzzd)		These services are required for making designing of consumer products, industrial products, packages, logos, graphics, website and corporate identity designing and production of three dimensional models. Without these services output services cannot be provided.
22	Development and supply of content service 65(105)(zzzb)		These services are required towards marketing efforts of the company concerned and as such have a clear nexus with the output activities.
23	Dry cleaning services 65(105)(zt)	Should not be allowed in case for personal use of employees.	Should be used only for office cleaning / maintenance.
24	Erection, commissioning or installation service 65(105)(zzd)	Should not be allowed in case for personal use of employees	These services rendered in connection with office premises or office equipment would have a direct nexus with the output activities.

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25	Event management service 65(105)(zu)	Should not be allowed in case services are procured as a staff welfare measure.	As per Circular 120/01/2010-ST dated 19 January 2010, it should not be for entertainment or staff welfare. However, in so far as it is for promotion of the business, it should be a valid input.
26	Fashion designing service 65(105)(zv)	Should not be allowed in case for personal use of employees.	Should be used only for office purposes.
27	Forward contract services 65(105)(zzy)		
28	General Insurance Service 65(105) (d)	Should not be allowed in case for personal use of employees; it is also not allowed in so far as it relates to a motor vehicle except when used for provision of a taxable service for which credit on motor vehicle is available as capital goods;	Should be used only for office purposes. This could include fixed assets insurance or group insurance for official activities.
29	Goods Transport operators 65(105)(zzp)	Should not be allowed in case for personal use of employees.	Should be used only for office purposes.
30	Information technology software service 65(105)(zzzze)		These services are availed for procuring the software for running the operation of company. As export of services is dependent on the better operation of company. Hence the software is an input for providing output service. In addition to this software is required for the data management
31	Intellectual property services 65(105)(z zr)		Should be used only for office purposes.
32	Interior decorator's services 65(105)(q)	Should be allowed if used for renovation or maintenance of office premises only.	
33	Internet telecommunication		A company uses the telecommunication /internet

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	services 65(105)(zzzu)		telecommunication services which are essential input services for providing output services. These input services are consumed essentially for providing the output services related to the export business and for discharging day to day duties by the administrative staff. Without the telephone and internet facility the services could not have been rendered.
34	Legal consultancy service 65(105)(zzzzm)	Should not be allowed in case for personal use of employees.	Should be used only for office purposes.
35	Management or Business consultant's services 65(105)		Consultancy Services are procured for providing advice, consultancy and technical assistance in relation to the business and therefore should be allowed.
36	Management, maintenance or repair service 65(105)(zzg)		A company procures services maintenance and repair of office premise, office equipments etc. The management, maintenance & repair service of office building is essential for conducting the business including exports.
37	Mandap keeper's services 65(105)(m)	Should not be allowed in case services are procured as a staff welfare measure.	As per Circular 120/01/2010-ST dated 19 January 2010, it should not be for entertainment or staff welfare. However, for activities relating to business, it should be allowed.
38	Manpower recruitment or supply agency's services 65(105)(k)		Procurement of manpower is a basic requirement of the industry and for which it has to engage recruitment agencies. The procurement of these services is essential in view of the high labor turnover and in order to identify the right person for the right job at the right time. An organization can't operate without appropriate people.
39	Market research agency's services 65(105)(y)		Required for business related activities.

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40	On-line information and database access or retrieval services 65(105)(zh)		A company does market analysis, studies economic factors and other market parameters for the purpose of providing output service. For this purpose online database and other research database are used.
41	Packaging services 65(105)(zzzf)		Should be allowed.
42	Pandal or shamiana contractor's service 65(105)(zzw)	Should not be allowed in case services are procured as a staff welfare measure.	As per Circular 120/01/2010-ST dated 19 January 2010, it should not be for entertainment or staff welfare. However, for activities relating to business, it should be allowed.
43	Photography services 65(105)(zb)	Should not be allowed in case services are procured as a staff welfare measure.	As per Circular 120/01/2010-ST dated 19 January 2010, it should not be for entertainment or staff welfare. However, for activities relating to business, it should be allowed.
44	Promotion or Marketing of Brand service 65(105)(zzzzq)		Should be allowed.
45	Public relation management service 65(105)(zzzs)		To maintain public relations, professionals are hired in maintaining relations with govt. authorities and organizations. Should be allowed
46	Rail travel agent's services 65(105)(zz)	Should not be allowed in case for personal use of employees.	Should be allowed for business use.
47	Real estate agent's services 65(105)(v)	Should not be allowed in case for personal use of employees.	Should be allowed for business use.
48.	Rent a cab service 65(105)(o)	It is not allowed in so far as it relates to a motor vehicle except when used for provision of a taxable service for which credit on motor vehicle is available as capital goods.	
49	Renting of immovable		The premises from where the party renders output services or

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	property services 65(105)(zzzz)		premises where books of accounts of company are maintained has been taken on rent and accordingly renting of immovable property is essential for operation for the output service.
50	Sale of space or time for advertisement services 65(105)(zzzm)		Should be allowed for business use.
51	Scientific or technical consultancy services 65(105)(za)		Should be allowed for business use.
52	Security agency's services 65(105)(w)	Should not be allowed when used for residential premises i.e. in case for personal use of employees.	The procurement of these services is essential for security of office buildings and equipment. Further, business operations involve handling of confidential data.
53	Service of permitting commercial use or exploration of any event organised by a person or organisation 65(105)(zzzzr)		Should be allowed for business use.
54	Service relates to short term accommodation 65(105)(zzzzw)	Should not be allowed in case for personal use of employees	Should be allowed for business use.
55	Sponsorship services 65(105)(zzzn)	Should not be allowed in case services are procured as a staff welfare measure.	As per Circular 120/01/2010-ST dated 19 January 2010, it should not be for entertainment or staff welfare. Should however be allowed for business use.
56	Steamer agent's services 65(105)(I)		Should be allowed.
57	Stock broker services 65(105)(a)	Should not be allowed in case for personal use of employees	Should be allowed for business use.
58	Storage and warehousing service		Should be allowed.

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	65(105)(zza)		
59	Survey and map-making service 65(105)(zzzc)		Should be allowed for business use.
60	Technical inspection and certification service 65(105)(zzi)		This input service is related to export of service which is mainly used for inspecting the items which are exported to other country at the ports and other places. Should be allowed for business use.
61	Technical testing and analysis service 65(105)(zzh)		Should be allowed for business use.
62	Telecommunication service 65(105)(zzzx)	Should not be allowed in case for personal use of employees.	Should be allowed for business use
63	Transport of coastal goods; and goods transported through inland water service 65(105)(zzzl)	Should not be allowed in case for personal use of employees	Should be allowed for business use
64	Transport of goods by air service 65(105)(zzn)	Should not be allowed in case for personal use of employees	Should be allowed for business use
65	Transport of goods by rail service 65(105)(zzp)	Should not be allowed in case for personal use of employees	Should be allowed for business use
66	Transport of goods by road service 65(105)(zpz)	Should not be allowed in case for personal use of employees	
67	Transport of passengers by air service 65(105)(zzzo)	Should not be allowed in case for personal use of employees.	Should be allowed for business use
68	Travel agent's service 65(105)(zzx)	Should not be allowed in case for personal use of employees.	Should be allowed for business use