

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

PRINCIPAL BENCH-COURT NO.1

Service Tax Appeal No. 50494 of 2019

(Arising out of Order-in-Appeal No. 24/COMMR/ST/JBP/2019 dated 10.01.2019
passed by the Commissioner, Central GST, Central Excise & Customs, Mission
Chowk, Napier Town, Jabalpur- 482001)

Madhya Pradesh Power Generating Co. Ltd.Appellant
S.G.T.P.S,
Birsingpur-484552

Versus

**The Commissioner, Central GST,
Central Excise & Customs, Mission Chowk,
Napier Town, Jabalpur 482001**Respondent

APPEARANCE:

Shri D.D. Rishi, Advocate for the appellant
Dr. Radhe Tallo, Authorized Representative of the Department

CORAM:

**HON'BLE MR. JUSTICE DILIP GUPTA, PRESIDENT
HON'BLE MR. P. ANJANI KUMAR, MEMBER (TECHNICAL)**

FINAL ORDER NO. 50711/2023

Date of Hearing: May 22, 2023

JUSTICE DILIP GUPTA

The order dated 10.01.2019 passed by the Commissioner ordering recovery of service tax under 73(2) of the Finance Act, 1994 with interest and penalty has been assailed in this appeal by Madhya Pradesh Power Generation Company Ltd¹.

2. The appellant is a State Government undertaking and the issue that arises for consideration in this appeal relates to levy of service tax on the amount deducted by the appellant from the

1 the appellant

vendors towards liquidated damages as they failed to supply the goods/execute the work within the stipulated time.

3. The order has confirmed the demand of service tax both for the period prior to 01.07.2012 and post 01.07.2012.

4. For the period prior to 01.07.2012 collection of amount towards liquidated damages was not included in any of the specified taxable services under any of the clauses of sub-section (105) of section 65 of the Finance Act, 1994². Thus, no service tax could have been levied on the amount of liquidated damages so collected.

5. For the period w.e.f. 01.07.2012, the impugned order has observed that as the appellant received the amount as consideration for the failure on the part of the contractors to honor the terms of the contract or violating the conditions of the contract, it would be taxable under clause (e) of section 66E of the Finance Act.

6. In **South Eastern Coalfields Vs. Commissioner of Central Excise and Service Tax**³, the Tribunal held that liquidated damages recovered on account of breach or non-performance of contract are not consideration in view of any service but are in the nature of deterrent imposed so that such a breach or non-performance is not repeated. The relevant paragraphs of the decision of the Tribunal are reproduced below:

"27. It is trite that an agreement has to be read as a whole so as to gather the intention of the parties. The intention of the appellant and the parties was for supply of coal; for supply of goods; and for availing various types of services. The consideration contemplated under the agreements was for such supply of coal, materials or for availing various types of services. The intention of the parties certainly was not for flouting the terms of the

2 The Finance Act

3 2020 (12) TMI 912-CESTAT, New Delhi

agreement so that the penal clauses get attracted. The penal clauses are in the nature of providing a safeguard to the commercial interest of the appellant and it cannot, by any stretch of imagination, be said that recovering any sum by invoking the penalty clauses is the reason behind the execution of the contract for an agreed consideration. It is not the intention of the appellant to impose any penalty upon the other party nor is it the intention of the other party to get penalized.

28. It also needs to be noted that section 65B(44) defines -service to mean any activity carried out by a person for another for consideration. Explanation (a) to section 67 provides that -consideration includes any amount that is payable for the taxable services provided or to be provided. The recovery of liquidated damages/penalty from other party cannot be said to be towards any service per se, since neither the appellant is carrying on any activity to receive compensation nor can there be any intention of the other party to breach or violate the contract and suffer a loss. The purpose of imposing compensation or penalty is to ensure that the defaulting act is not undertaken or repeated and the same cannot be said to be towards toleration of the defaulting party. The expectation of the appellant is that the other party complies with the terms of the contract and a penalty is imposed only if there is non-compliance.

29. The situation would have been different if the party purchasing coal had an option to purchase coal from 'A' or from 'B' and if in such a situation 'A' and 'B' enter into an agreement that 'A' would not supply coal to the appellant provided 'B' paid some amount to it, then in such a case, it can be said that the activity may result in a deemed service contemplated under section 66E (e).

30. The activities, therefore, that are contemplated under section 66E (e), when one party agrees to refrain from an act, or to tolerate an act or a situation, or to do an act, are activities where the agreement specifically refers to such an activity and there is a flow of consideration for this activity.

32. In the present case, the agreements do not specify what precise obligation has been cast upon the appellant to refrain from an act or tolerate an act or a situation. It is no doubt true that the contracts may provide for penal clauses for breach of the terms of the contract but, as noted above, there is a marked distinction between 'conditions to a contract' and 'considerations for a contract'.

7. The Circular dated 28.02.2023 issued by the Central Board of Indirect Tax and Customs also provides that service tax cannot be levied on the amount collected for the said purpose and it is reproduced below:

"4. As can be seen, the said expression has three limbs: -i) Agreeing to the obligation to refrain from an act, ii) Agreeing to the obligation to tolerate an act or a situation, iii) Agreeing to the obligation to do an act. Service of agreeing to the obligation to refrain from an act or to tolerate an act or a situation, or to do an act is nothing but a contractual agreement. **A contract to do something or to abstain from doing something cannot be said to have taken place unless there are two parties, one of which expressly or impliedly agrees to do or abstain from doing something and the other agrees to pay consideration to the first party for doing or abstaining from such an act. Such contractual arrangement must be an independent arrangement in its own right. There must be a necessary and sufficient nexus between the supply (i.e. agreement to do or to abstain from doing something) and the consideration.**

5. **The issue also came up in the CESTAT in Appeal No. ST/50080 of 2019 in the case of M/s Dy. GM (Finance) Bharat Heavy Electricals Ltd** in which the Hon'ble Tribunal relied on the judgment of divisional bench in case of M/s South Eastern Coal Fields Ltd Vs. CCE Raipur (2021 (55) G.S.T.L 549(Tri-Del)). Board has decided not to file appeal against the CESTAT order ST/A/50879/2022-CU[DB] dated 20.09.2022 in this case and also against Order A/85713/2022 dated 12.8.2022 in

case **of M/s Western Coalfields Ltd.** Further, Board has decided not to pursue the Civil Appeals filed before the Apex Court in M/s South Eastern Coalfields Ltd. supra (CA No. 2372/2021), M/s Paradip Port Trust (Dy. No. 24419/2022 dated 08-08-2022), and M/s Neyveli Lignite Corporation Ltd (CA No. 0051-0053/2022) on this ground.

6. **In view of above, it is clarified that the activities contemplated under section 66E(e), i.e. when one party agrees to refrain from an act, or to tolerate an act or a situation, or to do an act, are the activities where the agreement specifically refers to such an activity and there is a flow of consideration for this activity.** Field formations are advised that while taxability in each case shall depend on facts of the case, the guidelines discussed above and jurisprudence that has evolved over time, may be followed in determining whether service tax on an activity or transaction needs to be levied treating it as service by way of agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act. Contents of Circular No. 178/10/2022-GST dated 3rd August, 2022, may also be referred to in this regard."

(emphasis supplied)

8. It is, therefore, not possible to sustain the demand.

9. The order dated 10.01.2019 passed by the Commissioner, therefore, deserves to be set aside and is set aside and the appeal is allowed.

(Order dictated and pronounced in the open Court)

**(JUSTICE DILIP GUPTA)
PRESIDENT**

**(P. ANJANI KUMAR)
MEMBER (TECHNICAL)**