CUSTOMS, EXCISE AND SERVICE TAX APPELLATE TRIBUNAL MUMBAI

WEST ZONAL BENCH

SERVICETAX APPEAL NO: 87085 of 2017

[Arising out of Order-in-Original No: 01/STA-I/SN/17-18dated 29th May 2017passed by the Commissioner of Service Tax, Audit – I, Mumbai.]

BG Exploration & Production India Ltd
BH House, Hirandani Business Park, Lake Boulevard Road,
Powai, Mumbai – 400 076 …***Appellant***

versus

Commissioner of Service Tax (Audit-I)
8th Floor, Lotus Info Centre, Near Parel Railway Station
Parel (E), Mumbai – 400 012 ***…Respondent***

APPEARANCE:

Shri JH Motwani, Shri Kirti Bhoite, Shri Arihant Tater and M/s Divya Jaswant, Advocates for the appellant

Shri Bidhan Chandra, Additional Commissioner (AR) for the respondent

CORAM:

HON'BLE MR C J MATHEW, MEMBER (TECHNICAL)
HON'BLEDR SUVENDU KUMAR PATI, MEMBER (JUDICIAL)

FINAL ORDER NO: A/85785 / 2020

DATE OF HEARING: 30/08/2019
DATE OF DECISION: 11/06/2020

PER: C J MATHEW

At the root of this dispute brought before us by M/s BG Exploration & Production India Ltd is the fastening of tax liability by combination of the legal fiction in Finance Act, 1994 for deeming 'provider' and 'recipient' and of the inclusion of a particular business model within the compasses of that very fiction by way of a clarificatory circular of the Central Board of Excise & Customs that was deployed by the adjudicating authority to hold that the attribution of certain expenditure of the appellant to one of their business ventures sufficed for it to be ‘consideration’ for service rendered. Thereby, the appellant found themselves saddled, in order-in-original no. 01/STA-I/SN/17-18 dated 29th May 2017 of Commissioner of Service Tax, Audit-I, Mumbai, with demand of ₹ 10,98,62,116 confirmed under section 73 of Finance Act, 1994, along with applicable interest under section 75 of Finance Act, 1994, besides being imposed with penalty of like amount under section 78 of Finance Act, 1994 and further penalty under section 77 of Finance Act, 1994.

2. From the impugned order, it is seen that, in the initial engagement with the assessee, the tax authorities appeared to have got the wrong end of the stick; it is not the intent of any tax legislation that demand can originate in an *Explanation* and, that too, intended for expanding the scope of existing definition by resorting to legal fiction for overcoming a judicially erected barrier to imposition of a levy. As an adjunct of the principal provision, *Explanation* is to be read along with it and not as an autonomous provision to be invoked. That overreach at the genesis may well explain the tortuous reiteration of circulars and interpretations that, in the stages preceding the issue of show cause notice, were relied upon for attempting to

persuade the assessee of the superiority of departmental wisdom. It is in the nature of any tax investigation that multi-pronged justifications are offered as much for eluding liability as for staving off internal accountability and, unless relevant for application of the relevant legal provisions to ascertained facts, are to be relegated to the periphery. Citing of the decision of the Hon'ble Supreme Court in *Gammon India Ltd v. Commissioner of Customs, Mumbai [2011 (269) ELT (SC)]* is just one case in point; therein the appellate jurisdiction, invoked over disputed eligibility for import under a notification, issued in exercise of powers conferred by Customs Act, 1962, for availing exemption from duties subject to conditions, had rejected the proposition that exemption notifications deserve to be interpreted liberally and, it did not, as suggested by the adjudicating authority, demutualize joint-venture and its constituents for the purposes of Finance Act, 1994. The impugned order is replete with such digressive eruptions. The resultant obstruction of clear view of the issue to be resolved in adjudication is no less of obscuring fog before us.

3. The impugned order does invoke the power conferred under section 73 of Finance Act, 1994 for extending the period of demand to five years but, nevertheless, did not venture to saddle liability within one of the enumerated activities in section 65(105) of Finance Act, 1994 that was in force before 1st July 2012. That Revenue is not in appeal against this self-imposed restriction is tacit acceptance that

such activity was not taxable in the earlier regime. If that be so, the ingredients that justify invoking of the extended period, as well as imposition of penalty under section 78 of Finance Act, 1994, may well be absent and, particularly, as the clarification was issued only in September 2014. We, therefore, restrict ourselves to the legality of the levy for the normal period under the revised scheme of tax.

4. We have heard Learned Counsel for the appellant and Learned Authorized Representative at length, but as we are tasked with cutting a straight path through the conceptual commotion in the impugned order, we intend to turn to their submissions for assistance, to the extent of relevance, only after isolating the issue for resolution.

5. Among its several business undertakings, M/s BG Exploration and Production India Ltd is engaged in the exploration, development and production of hydrocarbons in the Panna-Mukta and the Mid-South Tapti fields within the framework of ‘production sharing contract (PSC)’ dated 22nd December 1994 entered into by the Government of India with M/s Oil & Natural Gas Corporation Ltd (ONGC), M/s Reliance Industries Ltd and themselves. Essentially, the monopoly over naturally occurring hydrocarbon resources, retained with the Central Government by constitutional prerogative, was offered to corporate entities - both domestic and foreign - for development and recovery in which the risks transferred to the contractors was compensated by ‘cost petroleum’ to be shared among the three before the Government of India was entitled to a share of ‘profit

petroleum' with the three co-venture partners.

6. *Vide* circular no. 179/5/2014-ST dated 24th September 2014, the Central Board of Excise & Customs clarified that, consequent upon broadening of taxable 'service' in the 'negative list' regime implemented from 1st July 2012, transactions between 'joint venture' and constituents of such 'joint venture', akin to the distinguishment of 'unincorporated association' or 'body of persons' from its members thereof as provided for in *Explanation 3(a),* below section 65B (44) of Finance Act, 1994 defining 'service', are also to be deemed as service provided for consideration and liable to tax under Finance Act, 1994. The 'production sharing contract (PSC)' envisaged the conducting of 'petroleum operations' through 'joint operating agreement' and, in accordance with the 'joint operating agreement', the 'employee benefit expenses' of ₹ 25,34,46,003, ₹ 39,19,68,072 and ₹24,34,37,994 were booked by the appellant for 2012-13 (from July 2012), 2013-14 and 2014-15 (up to December 2014) as manpower cost in deploying personnel, on full time or otherwise, for operations. It was on these amounts that liability under Finance Act, 1994 was sought to be recovered from the appellant on the premise of the *Explanation*, pertaining to 'unincorporated association' or 'body of persons', having been rendered applicable to 'joint ventures' too by the clarification.

7. It, therefore, devolves upon us to ascertain if the clarification

issued by Central Board of Excise & Customs is in harmony with the intent of *Explanation (3)* below section 65B (44) of Finance Act, 1994, if the 'joint operation agreement' is a 'joint venture' to which the clarification would apply and if it was correct to conclude that the expenditure booked by the appellant was consideration for rendering of taxable service. In view of the complexities involved, it may not be out of place to recall historical aspects relevant for proper appreciation of the contours of a dispute that is before the Tribunal for the very first time.

8. The artificial delineation of 'unincorporated associations' as well as 'body of persons' from the members thereof, by way of *Explanation* referred to *supra*, is not novel to the paradigm of 'negative list' regime but is a carryover from the legal fiction incorporated, under the erstwhile tax regime, in Finance Act, 1994 for overcoming the impediment of judicial affirmation of the principle of mutuality, originally enunciated by the Hon'ble Supreme Court in *Commercial Tax Officer v. Young Men's Indian Association [(1970) 1 SCC 462]* for relieving such bodies from the ambit of tax on sale of goods to its own members, to set aside demand of tax on services rendered by 'club or association' to its members. Thereafter, by amendment, through Finance Act, 2006, inserting

> *'Explanation – For the purposes of this section, taxable service includes any taxable service provided or to be provided by any unincorporated association or body of persons to members thereof, for cash, deferred payment or any other valuable consideration.'*

in section 65, the fiction of separability was enacted but, notwithstanding which, the activity continued to be held as non-taxable by judicial rulings. The circular that was relied upon in the impugned order maintained the enunciation that mutuality is no bar to taxation of such transactions.

9. That the contents of the said circular of the Central Board of Excise & Customs, directing that ‘joint ventures’ should also be subject to the very same demutualization as applicable to ‘unincorporated associations’ or ‘bodies of persons’, could not go beyond the *Explanation* did not appear to have weighed with the adjudicating authority. And that it was not within the competence of the adjudicating authority to stretch the clarification beyond the intendment of the *Explanation* also appears to have been overlooked. As ‘unincorporated association’ and ‘body of persons’ is conferred with legal recognition for the limited purpose of pursuing common objectives, the existence of its constituents, as persons, is never eclipsed either in relation to other entities or, for that matter, even with the common undertaking. In the several judgements that were drawn upon for arriving at the decision that the principle of mutuality was applicable to levy of service tax, it was the transaction originating from the ‘unincorporated association’ or ‘body of persons’ for catering to the needs of its members, and not the *contra*, that was in dispute and which impelled the insertion of the *Explanation* in section 65, as well as the successor section 65B, of Finance Act, 1994. Reliance on the clarificatory circular of Central Board of Excise & Customs is misplaced in the context of allegation herein that tax liability had not been discharged on service

rendered by appellant to the joint venture. We, therefore, do not propose to subject the said circular to the test of harmony with the *Explanation*.

10. According to Learned Authorized Representative, the appellant is a constituent, along with M/s Oil & Natural Gas Corporation and M/s Reliance Industries Ltd, in a joint venture, established for drilling and production of petroleum products and condensates, as evidenced by various documents and as this common purpose in conjunction with its juristic status conforms to the facets determined by the Hon'ble Supreme Court in *New Horizons Ltd v. Union of India [1995 SCC (1) 478]*. He, therefore, argues that recruitment, training and deployment of manpower for the joint venture is service within the meaning of section 65B (44) of Finance Act, 1994. Adverting to circular no. 148/17/2011-ST dated 13th December 2011 of Central Board of Excise & Customs which, relying upon decision of the Hon'ble Supreme Court in *re New Horizons Ltd*, clarified that agreement between two entities for rendering of services to a third party suffices to determine the emergence of a new entity, he urged us to apply it here for the resolution of present dispute.

11. We have no doubt that agreement among entities for rendering of service to another entity is the essence of 'joint venture'; however, it is doubtful if 'joint operation agreement', mandated by the terms of the 'production sharing contract', can be deemed to be one such in the absence of an external beneficiary. In the impugned contract, the several participating interests are, collegially, designated as 'contractor' in the

singular and in furtherance of the policy of the Government of India to involve corporate participation for efficient harnessing of natural resources as codified in the ‘production sharing contract’ agreed upon. This, then, would be the primary association as joint venture comprising of four entities, including Government of India, for viability in extraction of natural resource as the common goal. The manner in which the contract provides for distribution of ‘profit petroleum’ and ‘cost petroleum’ is a business model for ensconcing within itself the alienation of risk by the Government of India which necessarily mandates a working arrangement for the disaggregation of ‘cost petroleum’ as compensation for the mutually exclusive risks undertaken by the contractor. The participating interests in the ‘joint operations’ have not come together of their own accord for the common purpose of bearing the risk but from one stipulation in the contract setting forth the common purpose including the participation in the proceeds of ‘profit petroleum’ that is extracted. The ‘joint operations’ does not render service, within the meaning of section 65B(44) of Finance Act, 1994, as there is no beneficiary entity outside the ‘production sharing contract (PSC)’, to which ‘joint operations’ is subordinated, for determination as joint venture to which the *Explanation* could be applied. This looming presence of ‘production sharing contract’ to the exclusion of any other independent or subordinate agreement and the indispensability of the Government of India to such contracts has been ordained by the Hon’ble Supreme Court in *Reliance Natural Resources Ltd v. Reliance Industries Ltd [(2010) 7 SCC 1)].*

12. In its truest sense, service is the satisfaction of one's need by another person with the existence of a 'provider' as *sine qua non* in any service transaction and with accumulated capital affording the luxury of such satisfaction. Owing to increasing pressure on manufacturers to scale up size and to specialize in competencies for achieving cost optimality, that is no longer a luxury borne on affordability. With the maturing of this sector, the State inserted itself as a stakeholder and, as always, tax was, so to speak, the foot in the door. Taxpayer fatigue, engendered by prohibitively high rates, frenetic enforcement overreach and incessant adversarial litigation, was not conducive to direct implementation of the 'negative list'; more so, as definitional certitude was necessary to guide assesses and assessors through unfamiliar territory of intangibles. The addition of services to the enumeration, though slow in the early years, underwent a five-fold increase between 2000-01 and 2006-07 signposting the imminence of transition to 'negative list' regime. The adroit easing of the upgraded scheme into the sphere of tax administration was the outcome of carefully calibrated strategy to reach this goal. In the classificatory regime, adopted in the beginning, the definition of 'service', as enumerated series, did not reflect its essence, *viz*., substitution of self-performance with the descriptive limit further encapsulated in provider-recipient equation to which 'consideration', as measure of its value, was subordinated.

13. Under the 'negative list' regime, in which demarcation between services was superfluous, the obliteration of boundaries permitted the definition of 'service', as

> *'(44) …any activity carried out by a person for another for consideration, and includes a declared service, but shall not include - ..'*

in section 65B of Finance Act, 1994, to encompass all 'activities' save those exogenic to, and excepted in, it and aligned it with the essence of service by the expression 'for another', replacing 'to any person', to eliminate the recipient as a necessity. In the new scheme of tax, 'consideration', being the obligated recompense to the provider devolving on the person who opted for hiving off the undertaking of an activity, was no longer mere measure of value but translatable as the span of service rendered. Thus, 'service' was the extent of activity entrusted to a provider for such consideration as rendered it economically gainful to be outsourced. We now subject the expenditure booked by the appellant to test of conformity with this definition.

14. In *Cricket Club of India Ltd v. Commissioner of Service Tax, Mumbai [2015 (40) STR 973 (Tri-Mumbai)*, on examination of the several types of payments made to clubs by members, the Tribunal dealt with entrance fees, held to be akin to capital contribution, thus

> *'11….Consideration is, undoubtedly, an essential ingredient of all economic transactions and it is certainly consideration that forms the basis for computation of service tax. However, existence of consideration cannot be presumed in every money flow…. The factual matrix of the existence of a monetary flow combined with convergence of two entities for such flow cannot be moulded by tax authorities into a taxable event without identifying the specific activity that links the provider to the recipient.'*

before concluding that

> *'14….Each category of fee or charge, therefore, needs to be examined severally to determine whether the payments are indeed recompense for a service before ascertaining whether that identified service is taxable.*
>
> *xxx*
>
> *16…..Wages of employees and costs of running the establishment,…., are necessary expenses for such sustenance.…… Contribution to expenses cannot, by any stretch, be deemed to be consideration for any identified service rendered.'*

The principle thus espoused, and emphatically reiterated by the Tribunal in *Mormugoa Port Trust v. Commissioner of Central Excise [2017 (48) STR 69 (Tri-Mum)]* as

> *'16… the two had come together with the common objective of earning revenue by jointly rendering port services at Jetty Nos. 5A and 6A…We are therefore of the view that the agreement between the Assessee and SWPL is joint-venture between the two, where the two co-venture are jointly controlling a common activity and sharing the revenue therefrom.*
>
> *17……..whatever the partner does for the furtherance of the business of the partnership, he does so only for advancing his own interest as he has a stake in the success of the venture…..All the resources and contribution of a partner enter a common pool of resources required for running the joint enterprise and the such an enterprise is successful the partners become entitled to profits as a reward for the risks taken by them for investing their resources the venture....'*

found approval of the Hon'ble Supreme Court with dismissal of appeal of Revenue.

15. It is incumbent upon participants in collaborative undertaking to contribute capital for attainment of the common purpose. It is the nature of the undertaking, in terms of permanence and of purpose, that determines

the mode of contribution. In the impugned 'production sharing contract', Government of India brings in its rights over the resources, M/s Oil & Natural Gas Corporation handles contracts and documentation, M/s Reliance Industries Ltd manages financial and commercial requirements and the appellant vested with responsibility for technical operations. The deployment of personnel is in pursuance of that obligation. No business venture can function without capital and the by-passing of transubstantiation of accumulated capital, in the form of cash and bank balances, into these rights and competencies does not derogate from that. Hence, the activity undertaken by the appellant with its cost equivalence recorded in the books is nothing but capital contribution. The adjudicating authority has erred in concluding that the mechanism of 'cash call' prescribed in the 'joint operations agreement' is consideration for services; it is intended as the vehicle for contribution by the participating interests to the capital requirements of the venture. As such capital contributions are obligated for the establishment and operation of a business venture, it is not 'consideration' for rendering of any taxable service.

16. From our discussion *supra*, we find that it is parties to the 'production sharing contract' who constitute a joint venture and that the *Explanation* below section 65B (44), intended to cover supply of services to a constituent of 'unincorporated associations' or 'body of persons' by the latter is not relevant to the present dispute. Further, the fulfilment of obligation to contribute to the capital of the joint venture is beyond the scope of taxation under Finance Act, 1994

as it does not amount to consideration. The performance of such obligations is intended to serve itself and, thereby, the joint-venture. As the demand confirmed in impugned order is not on the consideration for rendering of a service, we are not required to decide on the other issues.

17. Accordingly, the impugned order is set aside and appeal allowed.

(Order pronounced in the open court on 11/06/2020)

(C J Mathew)
Member (Technical)

(Dr. Suvendu Kumar Pati)
Member (Judicial)

**/as*