CUSTOMS, EXCISE & SERVICE TAX APPELLATE TRIBUNAL
MUMBAI

WEST ZONAL BENCH

Service Tax Appeal No. 85705 of 2014

(Arising out of Order-in-Original No. 05/AC/COMMR/TH-II/ST/2013 dated 29.11.2013 passed by the Commissioner of Central Excise, Thane II)

M/s. ICICI Prudential Life Insurance Co Ltd. **…..Appellant**
1089, Appasaheb Marathe Marg,
Prabhadevi,
Mumbai

Vs.

Commissioner of Central Excise, Thane II **…..Respondent**
4th Floor, Navprabhat Chambers,
Ranade Road
Dadar (W), Mumbai

APPEARANCE:

Shri V. Sridharan, Advocate and Shri S.S. Gupta, Chartered Accountant for the appellant
Shri S.K. Mathur, Special Counsel (AR) for the respondent

CORAM: **Hon'ble Mr C J Mathew, Member (Technical)**
Hon'ble Mr Ajay Sharma, Member (Judicial)

FINAL ORDER No: A/85885 / 2022

DATE OF HEARING : 31.03.2022
DATE OF DECISION : 16.09.2022

PER: C J MATHEW

The issue in this appeal of M/s ICICI Prudential Life Insurance Co Ltd arises from the peculiarity of the taxation of insurance products under Finance Act, 1994 and, more particularly, of 'unit linked insurance policies (ULIP)' with its combination of risk coverage and investment opportunity. In this specific product, the contribution of the policyholder comprises premium towards risk coverage and 'segregated funds' with the latter designated in 'units' representing portfolio of instruments that are opted for by the policyholder from among those categorised as high, medium and low yields. In the scheme of Finance Act, 1994, tax on 'life insurance service' was introduced by insertion of (zx) in section 65 (105) of Finance Act, 1994 by section 149 of Finance Act, 2002 and brought into effect from 16th August 2002 by notification no. 8/2002-ST dated 1st August 2002 but with some exemptions under notification no. 9/2002-ST dated 1st August 2002 that was rescinded by notification no. 23/2004-ST dated 10th September 2004. At the same time, with effect from 16th May 2008, with the incorporation of (zzzzf) in section 65 (105) of Finance Act, 1994, the consideration from policyholder for 'management of investment under ULIP' was levied to tax and it is the leviability of tax on 'foreclosure charges', 'surrender charges' and 'policy reinstatement charges' for the period from 2008-09 to 2010-11 and for 2011-12 totalling ₹135,98,52,361/- that the appellant disputes. In relation to the management of investment of 'segregated funds', the appellant, in addition to the regular contribution of the policyholder, receives 'premium allocation charge', 'fund management charges' and 'funds setting charges' on which service tax has been duly discharged.

2. 'Surrender charge' is built upon encashment of units either partially or in full before the expiry of the policy. 'Foreclosure charges' arises upon discontinuance of payment of premium with the cash equivalent of the balance of units remaining after deducting the said charge. Under the regulatory system, it is necessary for the insurance company to place the policyholder on notice before terminating the policy and charging for foreclosure at which stage a policyholder may choose to revive the policy by payment of 'policy reinstatement charges' with commitment to resume the payment of premium at the contracted intervals. Admittedly, on these the appellant had not been discharging tax liability justifying such by the restricted scope of the 'taxable service' communicated in circular no. 334/12/2010-TRU dated 26th February 2010 of Central Board of Excise & Customs (CBEC) and that these charges are separately stipulated in the policy issued by the appellant to the holder.

3. Learned Senior Counsel appearing for the appellant informed that policies issued by insurance provides do, by and large, fall into three categories, viz., 'risk policy' dedicated only to risk coverage, 'endowment policy' covering risk and offering returns on investment and 'unit linked policies' that comprise premium for risk cover,

segregated funds that are invested on behalf of the holder and fund management charges. He pointed out that the present dispute pertains only to the last offering and that the issue in dispute can be traced to the tax variation pertaining to the several components that, taken together, is the sold as a product by the appellant to policy holders. Distinguishing the charges that are the nub of the dispute, Learned Senior Counsel contended that the proceedings are based on the assumption that surrender is a consequence of voluntary act on the part of the policy holder, that reinstatement is to the benefit of the policy holder and that non-payment of premium also has the consequence of release of invested funds to the holder. He relied upon the decisions of the Tribunal in *Max Life Insurance Co India Ltd v. Commissioner of Central Excise & Service Tax [2019 (8) TMI 967-CESTAT DELHI]* and in *Bharti AXA Life Insurance Co Ltd v. Commissioner of Service Tax-VI, Mumbai [2021 (7) TMI 735-CESTAT MUMBAI]*.

4. According to Learned Special Counsel, appearing for the respondent, the decisions cited by Learned Senior Counsel pertains only to 'surrender charges' which is entirely distinguishable from 'foreclosure charges' and contends that 'policy reinstatement charges' is in the nature of a fee which, in effect, enables the revival of the service contracted earlier but ceased to have effect by non-fulfilment of conditions of contract by the recipient of the service.

5. From the above, we find that the dispute is all about the applicability of 'management of investment under unit linked insurance policy', the impugned 'taxable service', to 'surrender charge', 'foreclosure charge' and 'reinstatement charge' recovered by the appellant from their customers during the period of dispute. The taxability of 'surrender charge' has already been determined by the Tribunal in *re Bharti AXA Life Insurance Co Ltd* which, after taking note the decision in *Shriram Life Insurance Company v. Commissioner of Customs, Central Excise & Service Tax, Hyderabad-IV [2019 (2) TMI 868-CESTAT HYDERABAD]* and in *re Max Life Insurance Co India Ltd*, held that

> *'9. It is common ground that upon an insured ceasing to comply with the obligation to pay the premium at stipulated intervals, the policy is deemed to be surrendered and the holder entitled to 'surrender value' representing the portion of the receipts that had been invested in the appropriate funds. There is also no dispute that the amount disbursed is lesser than the value of the funds on the date of surrender. The proposition of Learned Authorized Representative is that the amount so withheld is consideration for services rendered in connection with the fund during the period of investment. This, in our view, is far-fetched for the impugned service has already been subjected to levy under Section 65(105)(zzzzf) of Finance Act, 1994 till June, 2010 and under Section 65(105)(zx) of Finance Act, 1994 thereafter; if that were not so, the demand would not have been restricted only to the surrendered policies. Furthermore, as quid pro quo of service and consideration is essential for levy under Finance Act, 1994, the purported service rendered in the past would have to be subject to tax then notwithstanding the deferment of consideration till the surrender of policy. There would, thus, be no reason for*

surrender of the policy to be the trigger for discharge of duty liability with failure thereto empowering proceedings under Section 73 of Finance Act, 1994.

10. In re Shriram Life Insurance Company, the Tribunal examined the nature of 'surrender charge' before concluding that -

> *'11. …… In our view, the amounts entered as surrender/discontinuance charges in the appellant assessee's books of account are not consideration for any service rendered by them, but it represent the amount that is retained by insurer on the insured, exercises the right to receive the insurance money. The entirety of the transaction being that in actionable claim is outside the purview of the service tax and does not get covered under provisions of Finance Act, 1994.*
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> *12. While, it is true that the expression of 'Service' under Section 65B(44) only w.e.f. 1-7-2012, however, even for the period prior thereto the transaction in question is a actionable claim and not a service it has to be also noted that for the period prior to 1-7-2012, for an activity to be tax it had to qualify as a taxable service in one of the specified services. Since we are of the view, the transaction in question is not a service at all but the transaction in a actionable claim hence could not have been by any stretch of imagination covered under any of the specified taxable hence a service even for the period prior to 01.07.2012……*
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> *13. We are unable to agree with the Adjudicating Authority that the amounts recorded as surrender/discontinuance charges are consideration for services rendered and surcharges are designed to recoup the expenses already incurred towards procurement administration of the policy and incidental thereto. The finding of the Adjudicating Authority on premise entirely are incorrect reading of the IRDA (Treatment of Discontinuance Linked Insurance Policy) Regulations, 2010 and overlooking the first principle and fundamental position that for an activity to be taxed as service under provisions of Finance Act, 1994, the*

> *activity has to first qualify as a service. In our view, the regulations framed by IRDA with the aim of protecting of the insured by providing for a yardstick for computation for the surrender and the consequent discontinuance charges cannot be read and applied out the services rendered a transaction in an actionable claim, as a service, liable to be taxed under the provisions of Finance Act, 1994.'*

11. In re Max Life Insurance Co. Limited, an identical dispute before the Tribunal also considered the nature of 'surrender charge' to be -

> *'32. Having considered the rival contentions, we are satisfied that surrender charges are permitted to be levied by IRDA, by way of penal charges towards recovery of initial expenses incurred by the insurer in marketing and distribution of the policy. As IRDA has fixed limits as to recovery, which can be made from time to time from the initial cost, accordingly, IRDA have permitted to recover surrender charges in case of pre-mature policy, as per the table given hereinabove, so as to enable the insurer to recoup the cost incurred by them. Further, we find that legislators have clarified by substituting clause (ii) Explanation to Section 65(105)(zzzzf), clarified that service tax is levied only on the management fee or charges which are either fixed by IRDA or actually levied by the insurer, whichever is higher by substituting the explanation w.e.f. 1-7-2010....'*

12. In view of the conclusions in these decisions combined with our own observation supra, we find ourselves unable to be persuaded that a contrary view may have acceptance; more so, as Learned Authorized Representative has not been able to enlighten us with statute and precedent that may have been of assistance. His arguments, insofar as the decisions are concerned, is limited to these having followed the order of the Tribunal, now recalled, in re Reliance Life Insurance Company Ltd. and that the first of the two cited decisions, pending before the Hon'ble Supreme Court on appeal of Revenue, was in jeopardy as held by the judgment of the Hon'ble Supreme Court in Union of India v. West Coast Paper Mills Ltd.

> *[2004 (164) E.L.T. 375 (S.C.)] as was the decision of the Tribunal in re Reliance Life Insurance Company Limited in appeal before the Hon'ble High Court of Bombay.'*

6. We have no reason to take an alternative viewpoint insofar as 'surrender charge' in the present dispute is concerned. It has been pointed out by Learned Senior Counsel that 'foreclosure charge' is also no different from 'surrender charge' except that the former is the consequence of a positive decision to discontinue the policy while the latter stems from non-payment of 'premium' that has the effect of terminating the policy issued by the appellant. The consequence of such termination is identical to that of a voluntary closure of the policy beyond the threshold permissible in the insurance contract. The termination of contract of insurance, whether within the agreed upon terms and conditions or from a breach of conditions, closes the relationship between the provider and the recipient. Such closure erases the provider-recipient framework which is essential for the levy of service tax under Finance Act, 1994. Accordingly, we hold that the 'foreclosure charge' retained by the appellant is, in accord with the decision of the Tribunal in *re Bharti AXA Life Insurance Co Ltd*, not liable to tax under Finance Act, 1994.

7. As well as 'reinstatement charge' is concerned, the termination leading to 'foreclosure charge' is pre-empted by such payment upon issue of the mandatory notice prior to the erasure of the relationship

between the insurance company and the policyholder. The consequence of such notice and the response on the part of the policyholder, restores the relationship to that of provider and recipient. The charge cannot, therefore, be considered to be a preliminary before the relationship commences but is intended to facilitate the continuance of the relationship which was in jeopardy by non-compliance with the conditions of contract. The restoration of the relationship of provider-recipient is contingent upon such additional fee which cannot, in the circumstances of such restoration, be anything other than consideration for the continuance of 'taxable service' and, therefore, liable to service tax. The case of the appellant against the levy of tax on 'reinstatement charge' does not fit in with the matrix that excludes 'surrender charge' and 'foreclosure charge' from the ambit of tax. The impugned order cannot be faulted to that extent.

8. In view of findings *supra*, we set aside the demand of tax on 'foreclosure charge' and 'surrender charge' while upholding the tax liability of 'reinstatement charge' in the impugned order. The appellant contends that the extended period is not applicable to them and, thereby, should discharge them of tax liability as well as the consequent penalty. The appellant is engaged, and specialised, in insurance business. The nature of the charges levied from policyholders is most abundantly clear to them. The provisions of

section 65 of Finance Act, 1994 and section 65B of Finance Act, 1994 have no scope for doubt on the taxability and the failure to discharge the tax on ‘reinstatement charge’ cannot but be considered as deliberate evasion on their part. The justification offered for absence of intent to evade does not appear convincing. Therefore, the penalties arising from, and limited to, the ‘reinstatement charge’ is upheld. Appeal is, accordingly, disposed off.

(Order pronounced in open court on 16.09.2022)

(Ajay Sharma)
Member (Judicial)

(C J Mathew)
Member (Technical)

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