Customs, Excise & Service Tax Appellate Tribunal
West Zonal Bench at Ahmedabad

REGIONAL BENCH-COURT NO. 3

Service Tax Appeal No. 10622 of 2018 - DB

(Arising out of OIA-VAD-EXCUS-001-APP-833-2017-18 dated 24/01/2017 passed by Commissioner (Appeals) Commissioner of Central Excise, Customs and Service Tax-VADODARA-I)

Iant Educom Pvt Ltd **.....Appellant**
A/201, Manki Plaza, Near Indrapuri Atithi,
Waghodia Road, VADODARA
GUJARAT

VERSUS

Commissioner of C.E. & S.T.-Vadodara-i **.....Respondent**
1ST FLOOR...CENTRAL EXCISE BUILDING,
RACE COURSE CIRCLE,
VADODARA,
GUJARAT-390007

APPEARANCE:
Shri Dhruvank Parikh, Chartered Accountant, appeared for the Appellant
Shri Rajesh K Agarwal, Superintendent (AR) appeared for the Respondent

CORAM: HON'BLE MEMBER (JUDICIAL), MR. RAMESH NAIR
HON'BLE MEMBER (TECHNICAL), MR. C L MAHAR

Final Order No. 11687/2024

DATE OF HEARING: 05.07.2024
DATE OF DECISION: 30.07.2024

RAMESH NAIR

The brief facts of the case are that the appellant is engaged in the business of indigenously developed specialized training courses in computer education and is conducting specialized computer training programs. They are in possession of technical knowhow, expertise, information technology and in work relating to computer education throughout India. The appellant with the intention of establishing wide network of centers all over the country for conduct of training courses and with the purpose of expanding both of activity and business has offered franchise facility to different person or organization all over India. On expressing willingness to conduct said business under the name Institute of Advance Networking Technology (IANT),the appellant appointed various persons/organization to function as franchisee and they have entered into agreement with their franchisees on

the terms and conditions mentioned in the agreements. The appellant are discharging service tax on the franchise fees received from franchisee, however, they are engaging advertisement agencies for giving advertisement in newspaper and in other media for which they are paying the advertising charges to the advertising agencies. Part of advertising expenses is collected from their franchisee for the purpose of advertisement for which they have executed agreement of advertisement with their franchisee.

1.2 On the advertisement expenses incurred by the appellant and part of it collected from their franchisee were not being included in the value of service namely franchise service, therefore, a show cause notice dated 22.12.2016 was issued to the appellant proposing to demand service tax on the advertisement charges collected by the appellant from their franchisee on the ground that these advertisement charges should also be a part of gross value of franchisee service. In the show cause notice, the demand of service tax was proposed for the period 2012-2013 to 2015-2016 (upto May,2015). The Adjudicating Authority namely Additional Commissioner, Central Excise, Customs and Service Tax, Vadodara –I passed adjudication order whereby the proceeding in the show cause notice has been dropped on the ground that the advertisement charges collected from the franchisees is not a part of the gross value in respect of franchise service. The Revenue being aggrieved by the Order-In-Original, filed an appeal before Commissioner (Appeals) who vide impugned order dated 24.012015 allowed the revenue's appeal interpreting Rule 5 (1) of Service Tax (Determination of Value) Rules, 2006. Therefore, the present appeal.

2. Shri Dhruvank Parikh, Learned Chartered Accountant appearing on behalf of the Appellant at the outset submits that the entire order of the Commissioner (Appeals) is based on Rule 5 (1) of Service Tax

(Determination of Value) Rules, 2006. The Hon'ble Supreme Court in the case of Intercontinental Consultants & Technocrats Pvt Ltd in Civil Appeal No. 2013 of 2014 upholding the ruling given by the Hon'ble Delhi High Court whereby treating Rule 5 of Service Tax (Determination of Value) Rules, 2006 as unconstitutional as well as ultra vires, the provision of 66 and 67 of Chapter v of Finance Act, 1994, therefore, the entire order based on rule 5 which held ultra vires, the order will not sustain.

2.1 He further submits that the advertisement charges was collected from the franchisee as reimbursement because the said amount was paid to the advertisement agency. He submitted that the advertisement charges collected from the franchisee is not a part of value of franchise service. In support he placed reliance on the following judgments:-

- Aditya College of Competitive Examination vs. CCE – 2009 (22) STT 1- Bangalore CESTAT
- Agra Steel Corporation vs. CCE – 2009 (9) STT 580 –CESTAT
- CKP Mandal vs. CCE- 2006 (5) STT 1 –Bombay
- Commissioner of Central Excise , Ahmedabad vs. Nirma Ltd - 2005 (192) ELT 359.

3. Shri R.K Agarwal, Learned Superintendent (AR) appearing on behalf of the Revenue reiterates the finding of the impugned order.

4. We have carefully considered the submission made by both sides and perused the record. We find that the issue to be decided is for the purpose of gross value of franchise service, the cost of advertisement charges which is collected by the appellant as reimbursement expense is includible in the gross value of the franchise fees. We find that the show cause notice is based on the provision of Rule 5 (1) of Service Tax (Determination of Value) Rules, 2006. The relevant para of show cause notice is reproduced below:-

> *"10.2. Further in terms of provisions of Rule 5(1) of the Service Tax (Determination of Value) Rules, 2006, where any expenditure or costs are*

incurred by the service provider in the course of providing taxable service, all such expenditure or costs shall be treated as consideration for the taxable service provided or to be provided and shall be included in the value for the purpose of charging service tax on the said service. Therefore whereas the assessee showed to have incurred expenditure of Rs. 11,07,06,782/- purportedly on advertisements for their franchisee centres, in terms of the franchisee agreements said amount was includible in the total taxable value for the purpose of charging of service tax on the Franchisee services so provided by the assessee, however which was willfully not done by the assessee. Therefore an amount of Rs. 11,07,06,782/-, which escaped from assessment to service tax under category of franchisee services by acts of omission as above is liable to be charged to service tax."

4.1 As per the above paragraph of the show cause notice, the revenue sought to include the advertisement expense in the gross value of franchise service. Further, the adjudicating authority considering the Rule 5 of valuation Rules held that the advertisement expenses has to be borne by the franchisees on their own but as per the arrangement , the appellant are making payment of advertisement charges to the advertisement agencies and taking reimbursement from the service recipient, therefore, advertisement charges is not a part and parcel of the value of franchise service. Relevant para of the adjudication order is reproduced below:-

"22. Further, I find that Rule 5(1) of Valuation Rules, specifies that the expenditure or costs incurred by the service provider in course of providing taxable services are to be treated as consideration for the taxable services provided. In terms of these Rules, the costs incurred by the noticee for providing such advertisement services is to be considered as taxable services. As discussed above, it is not under dispute that the advertisement services were not being provided by the notice but were being provided by various advertising agencies. Thus, expenses for advertising were incurred by various advertising agencies and the noticee had paid to the said advertising agencies on behalf of the franchisee and subsequently collected reimbursement from its franchisees for such expenses. It is to be seen that whether such reimbursements could be treated as an additional consideration received by the noticee from its franchisees. In this regard I have gone through the agreement of the noticee entered with their franchisees. A sample terms and conditions related to preset issue are reproduced herein for reference:-

1. PERIOD

That the agreement shall be in force for a period of Two years with effect from dated 1 April 13 to date 31st March 15

2 FRANCHISEE FEE

(i) The Franchisee shall pay a sum of 4 lac (Four Lac Rupees only) non refundable individually as Franchisee fee for the period of Two years

(ii) …….

3. USE OF TRADEMARK AND LOGO OF IANT AND TIE-UP OF COMPANIES

4. MARKETING AND ADVERTISEMENT:

(i) The Franchisee is too bound for every quarterly Newspaper Advertisement and informs the students regularly regarding courses. And all expenses will be paid by their own; IANT will not contribute anything towards any such cost/expenses. Which is given by the Franchisee.

(ii) The franchisee is agreed to participate in advertisement budget of IANT for print media, electronic media or any other activity. The print media cost would be upto 12 lac p.a. per franchisee and franchisee is agree to give this participation amount with IANT.

(iii) The franchisee shall not have any objection if IANT take any media in any manner for the branding and promotion.

(iv) If in case and in any time if franchisee disagree for any budgeting for advertisement, so franchisee would be cancelled on immediate basis.

23. On perusal of the above terms and conditions it is observed that a franchisee were required to pay a non-refundable Franchisee fee as set out in the agreement, which is Rs. 4 lac for two years in the above case. Thus, the Franchisee fee to be paid by the franchisees was a non-refundable fee and it was to be retained by the notice.

24. It is also observed from the above terms and conditions, that the Franchisees were bound for quarterly newspaper advertisement and the expenses of such advertisement was to be paid by the franchisee itself and the noticee would not bear the cost of the same. In terms of this clause, no expenditure on advertisement was to be done by the noticee and all the expenses were required to be met by the respective franchisees themselves. However, for such advertisements, the franchisees were required to participate in advertisement budget of IANT for print/electronic media etc. and as per the agreement, the amount of budgetary expenses would cost upto Rs. 12 lakhs per annum, in the above case. In different franchisees, the estimated budgetary expenses mentioned in agreements for such advertisements is different. The Show Cause proposes to treat this amount as additional consideration since it was received by the noticee from their franchisees. The noticee in their contention have stated that the advertisement agencies have advised them to have one single point of collection of amount of advertisement and also showed that collective advertisement would be cheaper and would be in the interest of their company as well as the participant Franchisee Centers and that's why they decided to pay at a stretch from their own pocket first the amount pertaining to advertisement for all the Franchisee Centers and then claim a reimbursement of the same from the franchisee Centers. They have further contended that the said model of doing business was in the interest of them as well as the Franchisee Centers who mutually on large scale got the benefit of operating through the Cost Sharing Model by way of pooling of common resources required for expansion and promotion of the business. In this regard I find that it is a common trade practice to place common advertisements in print media so as to reduce the cost of advertisements and share the cost incurred while placing such advertisements. Thus, this is only a means adopted to reduce the expenses of the respective franchisees."

4.2 Challenging the Order-In-Original in the appeal filed by the Revenue before the Learned Commissioner (Appeals), the revenue has heavily relied upon the Rule 5 (1) of Service Tax (Determination of Value) Rules, 2006. The Commissioner (Appeals) in his order discussed in detail the provisions of Rule 5 of Service Tax (Determination of Value) Rules, 2006 and given finding as under:-

> *"5.2. The appellant department has contended that the action of the respondent is in violation of Clause (c) and (d) of the Explantion 1 to Rule 5(2) of the Service Tax (Determination of value) Rules, 2006. On the contrary, I find the respondent (M/s IANT) had rebutted in their detailed Cross Objections filed against the Grounds of Appeal that they were merely functioning as a 'pure agent' in the matter and no additional fees or profits or consideration for such Pure agent services is received by the appellant as defined under Rule 5(2) of Service Tax(Determination of value) Rules, 2006. However I find that the Department's view is worth reckoning as it is apparent from the fact that the respondent had allowed use of their brand name "IANT" under franchisee model to their various franchisees located in different parts of India and against these have received Franchise Fees. This is clearly in violation of Clause (C)of Rule 5(1) cited above. The respondent had given advertisement in the media all over India with the same pattern of promoting their brand and for creating awareness for students regarding the courses offered by them. Also, the respondent had shared the "Advertisement Budget" with all the franchisees as is evident from the "Marketing and Advertisement Agreements" entered by them with various franchisees, thus violating Clause (d) of Rule 5(1) of Service Tax(Determination of value) Rules, 2006. Thus, the argument of the respondent that they were acting as "Pure agent" is highly misplaced. This is further supported by the fact that the respondents have also paid advertisement charges to the media, which is an input service and have received amount from their franchisees in the name of Advertisement Charges. However they have failed to pay the Service Tax on the Advertisement Charges despite the clear provisions of Rule 5(1) of the Service Tax(Determination of value) Rules, 2006. Thus I find Department is quite justified in putting forth the plea that in view of clear mandate of Rule 5(1) of Service Tax(Determination of value) Rules, 2006 , any expenditure or costs which are incurred by the service provider in the course of providing taxable services are to be included in the value for the purpose of charging service tax on such services and I allow the Departmental plea on this point."*

4.3 In view of the above, we find that right from show cause notice upto the Commissioner (Appeals) order, the entire case of the Revenue is based on Rule 5 (1) & 5(2) of Service Tax (Determination of Value) Rules, 2006, we find that this Rule 5 (1) has been held unconstitutional as the same ultra vires the provision of section 66 and 67of the Finance Act, 1994, therefore, on this change of legal position as per the Hon'ble Apex Court

judgment, the entire action of the revenue is vitiated. Consequently, the order of the Commissioner (Appeals) is also not sustainable on this ground alone.

4.4 Without prejudice to the above, even if we ignore Rule 5, the valuation is governed by Section 67 which provides that only service charges recovered towards providing of service shall be taxable. In the present case, the advertisement is in the business interest of the franchisee but the arrangement of advertisement is such that the advertisement agencies are providing advertisement for the franchisee and the payment therefore is made by the appellant and the same is collecting as reimbursement from the franchisee. Therefore, the advertisement is the obligation of the franchisee and they were supposed to bear the expenses of advertisement but merely because first the advertisement charges is paid by the appellant to advertising agencies and subsequently recovered the same amount from the franchisee will not amount to provide the service by the appellant to the extent it relates to advertising expense. The advertising expenses is ultimately borne by the franchisee because the same is part of their business expenses, the same cannot be included in the gross value of franchise service. Therefore, we are in completed agreement with the finding given by the adjudicating authority and the same is upheld.

5. Consequently the impugned order allowing the revenue's appeal is not sustainable in law and in the fact. Hence, the same is set aside. Appeal is allowed with consequential relief.

(Pronounced in the open court on 30.07.2024)

(RAMESH NAIR)
MEMBER (JUDICIAL)

(C L MAHAR)
MEMBER (TECHNICAL)

Bharvi