

Tax Hotline

April 05, 2003

UNCERTAINTY OVER APPLICABILITY OF SERVICE TAX: CLARIFICATION SOUGHT

Taking into account the growing contribution of services to the Indian GDP, the Government of India ("GOI") first introduced indirect tax on services as a part of Finance Bill 1997. Since then subsequent Finance Bills have widened the scope of service tax by progressively adding new services every year. The Finance Bill, 2003 ("Bill") has kept up with this legacy and added 7 new services and broadened the application of 3 existing ones. The Bill has also proposed to enhance the service tax rate from the present 5% to 8%, but it is the withdrawal of exemption from service tax for proceeds received in foreign exchange this year that has led to a lot of confusion and anxiety amongst the service providers.

Service exporters were exempt from service tax vide the Government notification dated April 9, 1999. This covered services rendered to foreign clients outside India and also services provided for projects of foreign companies in India against payment in foreign exchange. This was much appreciated by the industry and regarded as being in line with the general principle followed in India and other countries of not levying local taxes on exports.

The GOI, vide notification dated March 31, 2003, has rescinded the aforementioned exemption and thus making all service exports chargeable to service tax with effect from April 1, 2003. Elimination of this exemption will have serious ramifications on the export sector as a whole and specifically on software and ITES/BPO service providers, engineering and management consultants, project exports, chartered and cost accountants, tour operators, securities and forex brokers and broadcasters.

Tax consultants state that the GOI has no intention to tax exports and this notification could be in fact an oversight on the part of the GOI. In fact the revenue officials clarified in a leading Indian financial daily that this notification would not apply to provision of services across Indian borders but to forex-earning services that are rendered within the domestic tariff area. However, the language of the notification does not support this view, thus leading to confusion amongst the exporters who are unclear on whether to include the service tax in their invoices. The Confederation of Indian Industry has made a representation to the GOI to withdraw this notification and restore the exemption. Until then the uncertainty would continue. Unless this exemption is withdrawn retrospectively, the exporters would still be liable for service tax for the interim period i.e. April 1, 2003 till the date of withdrawal. Further, if the exemption is not withdrawn and the Bill is enacted in its present form then the exporters would have to also collect the additional 3% from April 1, 2003.

Separately, please note that to enable levy of tax on services, an amendment to the Constitution is proposed (the 95th amendment bill has already been placed before the Parliament for ratification). This Constitutional amendment, and the consequent legislation would give the GOI the power to levy the tax and both the GOI and the State Governments sufficient powers to collect the proceeds.

Source: *The Economic Times*, April 4, 2003.

DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.

Research Papers

Decoding Downstream Investment

August 27, 2025

Mergers & Acquisitions

July 11, 2025

New Age of Franchising

June 20, 2025

Research Articles

2025 Watchlist: Life Sciences Sector India

April 04, 2025

Re-Evaluating Press Note 3 Of 2020: Should India's Land Borders Still Define Foreign Investment Boundaries?

February 04, 2025

INDIA 2025: The Emerging Powerhouse for Private Equity and M&A Deals

January 15, 2025

Audio

CCI's Deal Value Test

February 22, 2025

Securities Market Regulator's Continued Quest Against "Unfiltered" Financial Advice

December 18, 2024

Digital Lending - Part 1 - What's New with NBFC P2Ps

November 19, 2024

NDA Connect

Connect with us at events, conferences and seminars.

NDA Hotline

Click here to view Hotline archives.

Video

Nishith Desai Unplugged - Law, AI & the Future

August 20, 2025

Webinar : Designing Innovative Share Swap and Deferred

**Consideration Structures for PE and
M&A Deals**

July 15, 2025

**Webinar: Blended Finance
Structures to Scale up Climate
Smart Agriculture**

July 03, 2025