IN THE CUSTOMS, EXCISE & SERVICE TAX APPELLATE TRIBUNAL, NEW DELHI

PRINCIPAL BENCH, COURT NO.3

Service Tax Appeal No.51138 of 2020

(Arising out of Order-in-Appeal No. 255(CRM)CE/JDR/2020 dated 31.07.2020 passed by Commissioner (Appeals), Central Excise & CGST, Jodhpur.)

M/s. Hindustan Zinc Ltd.
(Yashad Bhawan, Udaipur (Raj.))

Appellant

VERSUS

Commr. of CGST & Central Excise, Udaipur
(142-B, Hiran Magri, Sec-11, Udaipur (Raj.))

Respondent

APPEARANCE :

Shri Shivam Bansal and Shri Dhruv Anand, Advocates for the Appellant
Shri Shashank Yadav, Authorized Representative for the Respondent

CORAM:
HON'BLE MS. BINU TAMTA, MEMBER (JUDICIAL)
HON'BLE MR. RAJEEV TANDON, MEMBER (TECHNICAL)

FINAL ORDER NO. 51039/2025

Date of Hearing : 6th June 2025
Date of Pronouncement : **17.07.2025**

Per Rajeev Tandon

The appellant is manufacturer of High Grade Zinc, Cadmium, Sulphuric Acid etc. and was also registered with the Service Tax Department for providing/receiving services of goods transport agency, manpower recruitment/supply agency, works contract and legal consultancy amongst others. The appellant is aggrieved of the impugned Order-in-Appeal dated 31st July 2020 whereby the Learned Commissioner (Appeals) upheld the Service Tax demand on "Misc. Income-EMD/Security Forfeited, Miscellaneous Income-Settlement-Fines/Penalties from the contractors, Misc. Income-Liquidated damages" along with interest and penalties under Section 75, Section 76 and Section 77 of the Finance Act, 1994.

2. The short question that arises for consideration in the present appeal is concerned with amounts collected by the appellant in the form of fines/penalties, liquidated damages, forfeiture of earnest money/security deposits etc. from the contractors who failed to provide the services within the agreed stipulated time/standards. During the course of audit of the appellant's records, an amount of Rs. 1,39,59,368/- was found to be collected by the appellants towards the said heads. The department alleged that the said amount was collected in lieu of 'tolerating the act' of service providers/contractors for poor performance or not meeting the obligations in full i.e. lesser than the contractual obligations/requirements. Out of the aforesaid amount confirmed by the authority below, a demand of Service Tax for Rs.5,90,451/- pertains to such retained/collected amounts on account of fines/penalties, security deposit/earnest money forfeited and liquidated damages as recovered from the contractors. The balance amount of Service Tax demand confirmed amounting to Rs. 11,20,080/- on unclaimed amounts was dropped by the learned Commissioner (Appeals). The moot question therefore, involved in the present appeal concerns leviability and chargeability the Service Tax under Section 66E(e) of the Finance Act, 1994 on the aforesaid sums retained/collected by the appellant. Section 66 E(e) reads as under:-.

> ***SECTION 66E. Declared services. —***
>
> *The following shall constitute declared services, namely:—*
>
> *(a) ……*
>
> *(b) ……*
>
> *(C)……*
>
> *(d)……..*
>
> *(e) agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act;*
>
> *(f)……*
>
> *(g)……..*
>
> *(h)……..*
>
> *(i)……..*
>
> *(j)……*

3. A show cause notice was issued to the appellant for the period April 2014 to March 2016 and April-June 2016, alleging the amounts collected by the appellant in the form of fines/penalties, liquidated damages, forfeiture of earnest money/security deposits etc. from the contractors who failed to provide the services within the agreed stipulated time etc., was in lieu of 'tolerating the act' of service providers/contractors like poor performance or not meeting the obligations and was therefore, chargeable to service tax amounting to Rs.20,93,905/- as the services rendered would fall under Section 66E(e) of the Act. The Adjudicating Authority vide order dated 21.12.2018 confirmed the demand of Rs.17,10,532/- alongwith interest and dropped the remaining amount of Rs.3,83,373/-. The appeal filed by the appellant however confirmed the amount aforestated while the rest of the demand was dismissed by the Commissioner (Appeals). Hence, the present appeal has been filed before this Tribunal.

4. Heard both sides and perused the records of the case.

5. The Learned Counsel Sri Shivam Bansal for the appellant submits that the issue involved in the present appeal i.e. whether the amounts collected by the appellant in the nature of forfeiture of security deposits/earnest money and fines/penalties etc. against delayed completion of works is chargeable to service tax under Section 66E(e) of the Finance Act, 1994, is no more res integra. He submits that the issue has been settled in their own case by the Tribunal in (i) Service Tax Appeal No. 52267 of 2019 CESTAT & (ii) Service Tax Appeal No. 51462 of 2019 CESTAT, New Delhi vide Final Order No. (i) 50025/2025 dated 1.1.2025 (ii) 59733/2024 dt. 4.11.2024 respectively.

6. We find that the issue has since been settled. The above referred decisions of the CESTAT, in the appellant's own case, relied on the Tribunal decision in the case of **South Eastern Coalfields Ltd Vs. CCE & ST, Raipur (2021 (55) GSTL-549 (Tri. Delhi)**. The observations of the Tribunal in the said case are as follows:-

"25. It is in the light of what has been stated above that the provisions of Section 66E(e) have to be analyzed. Section 65B(44) defines service to mean any activity carried out by a person for another for consideration and includes a declared service. One of the declared services contemplated under Section 66E is a service contemplated under clause (e) which service is agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act. There has, therefore, to be a flow of consideration from one person to another when one person agrees to the obligation to refrain from an act, or to tolerate an act, or a situation, or to do an act. In other words, the agreement should not only specify the activity to be carried out by a person for another person but should specify the :

(i) consideration for agreeing to the obligation to refrain from an act; or

(ii) consideration for agreeing to tolerate an act or a situation; or

(iii) consideration to do an act.

26. Thus, a service conceived in an agreement where one person, for a consideration, agrees to an obligation to refrain from an act, would be a „declared service" under Section 66E(e) read with Section 65B(44) and would be taxable under Section 68 at the rate specified in Section 66B. Likewise, there can be services conceived in agreements in relation to the other two activities referred to in Section 66E(e).

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 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.

43. It is, therefore, not possible to sustain the view taken by the Principal Commissioner that penalty amount, forfeiture of earnest money deposit and liquidated damages have been received by the appellant towards "consideration" for "tolerating an act" leviable to service tax under Section 66E(e) of the Finance Act."

7. As per order of the apex court dated 11.07.2023 in CA No. 2372/2021 (CCE & ST Vs South Eastern Coalfields Ltd.), it is clear that the Revenue did not pursue the appeal challenging the said decision of the Tribunal and the appeal initially filed was withdrawn upon a statement made by the learned ASG that he had instructions to withdraw the appeal. Thus the decision of the Tribunal in South Eastern Coalfields is the law laid down, which has a binding precedent and needs to be adhered to.

8. We also note that in a slew of cases, some of which are noted below, the subject issue is settled as aforesaid.

- Hindustan Zinc Limited v. Commissioner of Central Goods, Service Tax and Central Excise, Customs, Udaipur, Final Order No. 50519/2024 dated 25.4.2025 in Service tax Appeal No. 51497 of 2019-CESTAT New Delhi
- Oil & Natural Gas Corporation Ltd. Versus Commissioner of Central Goods & Service Tax, Dehradun, Final Order No.

50415/2025 dated 18.3.2025 in Service Tax appeal No. 52596 of 2019-CESTAT New Delhi

- Bharat Aluminium Company Limited v. Principal Commissioner of Central Tax, & Central Excise, Raipur, Final Order No. 50128/2024 dated 17.1.2024 in Service Tax Appeal No. 50800 of 2020 (DB)-CESTAT New Delhi
- Sarda Energy & Minerals Ltd. v. Principal Commissioner, Central GST, Central Excise & Customs, Raipur (C. G.), Final Order No. 50757/2023 dated in Service Tax Appeal No. 51699 of 2017-CESTAT New Delhi.

9. What emerges therefrom is that a consistent view has been taken by courts that the amount charged, necessarily has to be a consideration for the taxable service provided under the statute and the amount which has no nexus with the taxable service is not a consideration for the service provided and therefore, would not become a part of the value of the service which is taxable. Such amounts have been held to be in the nature of penal charges on account of breach or non-performance of contractual obligations or non-adherence to contractual stipulations and are recovered with the intention to make good for the losses suffered and to act as a deterrent to ensure that the buyer or the supplier do not violate the terms of the contract entered into. These amounts cannot be termed as a 'consideration' in lieu of rendering of a service under Section 65B (44) of the Act. Further, it has been laid down that for an activity to be covered as a "Declared Service" under Section 66E of the Act, there must necessarily be an independent agreement to refrain or tolerate or to do an act between the parties concerned.

10. The Department has also issued **Circular No.214/1/2023-ST dated 28.02.2023** analysing the provisions of Section 66E(e) read with 65B(44) of the Finance Act, 1994 and clarified that the activities contemplated under Section 66E(e) of the act ibid, were those where one party agrees to refrain from an act, or to tolerate an act or a situation, or to do an act. These are the activities where the agreement

specifically refers to such an activity and there is a flow of consideration for this activity. The said position had been clarified at great length by CBIC vide its Circular number **178/10/22-GST dt. 3.8.2022**, wherein it had gone into various associated aspects. Relevant extract thereof pertaining to liquidated damages, penalties imposed, cancellation charges, etc. are extracted below:-

> ***Liquidated Damages***
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> *7.1 Breach or non-performance of contract by one party results in loss and damages to the other party. Therefore, the law provides in Section 73 of the Contract Act, 1972 that when a contract has been broken, the party which suffers by such breach is entitled to receive from the other party compensation for any loss or damage caused to him by such breach. The compensation is not by way of consideration for any other independent activity; it is just an event in the course of performance of that contract.*
>
> *7.1.1 It is common for the parties entering into a contract, to specify in the contract itself, the compensation that would be payable in the event of the breach of the contract. Such compensation specified in a written contract for breach of non-performance of the contract or parties of the contract is referred to as liquidated damages. Black's Law Dictionary defines 'Liquidated Damages' as cash compensation agreed to by a signed, written contract for breach of contract, payable to the aggrieved party.*
>
> *7.1.2 Section 74 of the Contract Act, 1972 provides that when a contract is broken, if a sum has been named or a penalty stipulated in the contract as the amount or penalty to be paid in case of breach, the aggrieved party shall be entitled to receive reasonable compensation not exceeding the amount so named or the penalty so stipulated.*
>
> *7.1.3 It is argued that performance is the essence of a contract. Liquidated damages cannot be said to be a consideration received for tolerating the breach or non-performance of contract. They are rather payments for not tolerating the breach of contract. Payment of liquidated damages is stipulated in a contract to ensure performance and to deter non-performance, unsatisfactory performance or delayed performance. Liquidated damages are a measure of loss and damage that the parties agree would arise due to breach of contract. They do not act as a remedy for the breach of contract. They do not restitute the aggrieved person. It is further argued that a contract is entered into for execution and not for its breach. The liquidated damages or penalty are not the desired outcome of the contract. By accepting the liquidated damages, the party aggrieved by breach of contract*

cannot be said to have permitted or tolerated the deviation or non-fulfilment of the promise by the other party.

7.1.4 In this background a reasonable view that can be taken with regard to taxability of liquidated damages is that where the amount paid as 'liquidated damages' is an amount paid only to compensate for injury, loss or damage suffered by the aggrieved party due to breach of the contract and there is no agreement, express or implied, by the aggrieved party receiving the liquidated damages, to refrain from or tolerate an act or to do anything for the party paying the liquidated damages, in such cases liquidated damages are mere a flow of money from the party who causes breach of the contract to the party who suffers loss or damage due to such breach. Such payments do not constitute consideration for a supply and are not taxable.

7.1.5 Examples of such cases are damages resulting from damage to property, negligence, piracy, unauthorized use of trade name, copyright, etc. Other examples that may be covered here are the penalty stipulated in a contract for delayed construction of houses. It is a penalty paid by the builder to the buyers to compensate them for the loss that they suffer due to such delayed construction and not for getting anything in return from the buyers. Similarly, forfeiture of earnest money by a seller in case of breach of 'an agreement to sell' an immovable property by the buyer or by Government or local authority in the event of a successful bidder failing to act after winning the bid, for allotment of natural resources, is a mere flow of money, as the buyer or the successful bidder does not get anything in return for such forfeiture of earnest money. Forfeiture of Earnest money is stipulated in such cases not as a consideration for tolerating the breach of contract but as a compensation for the losses suffered and as a penalty for discouraging the non-serious buyers or bidders. Such payments being merely flow of money are not a consideration for any supply and are not taxable. The key in such cases is to consider whether the impugned payments constitute consideration for another independent contract envisaging tolerating an act or situation or refraining from doing any act or situation or simply doing an act. If the answer is yes, then it constitutes a 'supply' within the meaning of the Act, otherwise it is not a "supply".

7.1.6 If a payment constitutes a consideration for a supply, then it is taxable irrespective of by what name it is called; it must be remembered that a "consideration" cannot be considered de hors an agreement/contract between two persons wherein one person does something for another and that other pays the first in return. If the payment is merely an event in the course of the performance of the agreement and it does not represent the 'object', as such, of the contract then it cannot be considered 'consideration'. For example, a contract may provide that

payment by the recipient of goods or services shall be made before a certain date and failure to make payment by the due date shall attract late fee or penalty. A contract for transport of passengers may stipulate that the ticket amount shall be partly or wholly forfeited if the passenger does not show up. A contract for package tour may stipulate forfeiture of security deposit in the event of cancellation of tour by the customer. Similarly, a contract for lease of movable or immovable property may stipulate that the lessee shall not terminate the lease before a certain period and if he does so he will have to pay certain amount as early termination fee or penalty. Some banks similarly charge pre- payment penalty if the borrower wishes to repay the loan before the maturity of the loan period. Such amounts paid for acceptance of late payment, early termination of lease or for pre-payment of loan or the amounts forfeited on cancellation of service by the customer as contemplated by the contract as part of commercial terms agreed to by the parties, constitute consideration for the supply of a facility, namely, of acceptance of late payment, early termination of a lease agreement, of prepayment of loan and of making arrangements for the intended supply by the tour operator respectively. Therefore, such payments, even though they may be referred to as fine or penalty, are actually payments that amount to consideration for supply, and are subject to GST, in cases where such supply is taxable. Since these supplies are ancillary to the principal supply for which the contract is signed, they shall be eligible to be assessed as the principal supply, as discussed in detail in the later paragraphs.

Compensation for cancelation of coal blocks

7.2 In the year 2014, coal block/mine allocations were cancelled by the Hon'ble Supreme Court vide order dated 24-9-2014. Subsequently, Coal Mines (Special Provisions) Act, 2015 was enacted to provide for allocation of coal mines and vesting of rights, title and interest in and over the land and mines infrastructure together with mining leases to successful bidders and allottees. In accordance with Section 16 of the said Act, prior (old) allottee of mines were given compensation in the year 2016 towards the transfer of their rights/ titles in the land, mine infrastructure, geological reports, consents, approvals etc. to the new entity (successful bidder) as per the directions of Hon'ble Supreme Court.

7.3 No supplier wants a cheque given to him to be dishonoured. It entails extra administrative cost to him and disruption of his routine activities and cash flow. The promise made by any supplier of goods or services is to make supply against payment within an agreed time (including the agreed permissible time with late payment) through a valid instrument. There is never an implied or express offer or willingness on part of the supplier that he would tolerate deposit of an invalid, fake or unworthy instrument of payment against consideration in the form of cheque dishonour fine or penalty. The fine or penalty that the supplier or a banker

imposes, for dishonour of a cheque, is a penalty imposed not for tolerating the act or situation but a fine, or penalty imposed for not tolerating, penalizing and thereby deterring and discouraging such an act or situation. Therefore, cheque dishonor fine or penalty is not a consideration for any service and not taxable.

Penalty imposed for violation of laws

7.4 Penalty imposed for violation of laws such as traffic violations, or for violation of pollution norms or other laws are also not consideration for any supply received and are not taxable, which are also not taxable. Same is the case with fines, penalties imposed by the mining Department of a Central or State Government or a local authority on discovering mining of excess mineral beyond the permissible limit or of mining activities in violation of the mining permit. Such penalties imposed for violation of laws cannot be regarded as consideration charged by Government or a Local Authority for tolerating violation of laws. Laws are not framed for tolerating their violation. They stipulate penalty not for tolerating violation but for not tolerating, penalizing and deterring such violations. There is no agreement between the Government and the violator specifying that violation would be allowed or permitted against payment of fine or penalty. There cannot be such an agreement as violation of law is never a lawful object or consideration. The service tax education guide issued in 2012 on advent of negative list regime of services explained that fines and penalties paid for violation of provisions of law are not considerations as no service is received in lieu of payment of such fines and penalties.

11. In view of the above clarification and the law as settled by the Courts, the amounts in question cannot be held as a consideration for providing any services. Any amount recovered by the appellant per se cannot be so understood for rendering of service. For an amount to qualify as consideration there has to be *quid pro quo* or performance of an activity for consideration. So far as these amounts are concerned, no activity against the said amounts has been actually undertaken. There is therefore no rendering of service in terms of Section 65B (44) of the Finance Act, 1994 and therefore, no demand in terms of Section 66 E(e) of the act would be maintainable.

12. The present case is squarely covered by the various decisions of the Tribunal as referred herein above. Besides in the appellant's own case referred earlier in the order, the issue has since been settled. Following the same, we hold that the amounts in question as confirmed

by the lower authority, were certainly not towards rendition of any service, hence not leviable to service tax. The order of the lower authority can therefore not be sustained and is therefore set aside. The appeal filed is allowed with consequential relief if any as per law.

(Pronounced in the open court on **17.07.2025**)

(Rajeev Tandon)
Member (Technical)

(Binu Tamta)
Member (Judicial)

Pooja