

CENVAT credit on deposits insurance - Banks v/s Departments

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Introduction:

Banks are registered under service tax in the category of 'Banking and Financial Services'. They collect and pay service tax on its various incomes such as commissions, bank charges, documentation charges, processing fees etc. levied on its customers. However, one of the major revenue earned by the bankers is in the form of interest which is outside the purview of service tax as the same is covered in the negative list.

Issue:

Rule 6(3B) of the CENVAT Credit Rules, 2004, specifies that banking companies have an option to pay CENVAT credit proportionately @ 50% instead of paying based on actual. Many banks prefer this option as it is easy and leaves less scope for errors and interpretational issues. Since, individually identifying the eligible and ineligible input services based on nexus is practically difficult and could see legal challenge.

One of the items of dispute by the revenue is the availment of CENVAT credit by the bankers on the insurance premium paid for insuring the deposits accepted by them from various deposit holders viz., Fixed Deposits, Savings, Current etc. It is pertinent to note that insurance of these deposits is needed, as any slip up on its investment directly effects banks exposure. Since the quantum is huge and the risk is high, it is mandatory as per RBI guidelines that all banks must mandatorily take the insurance of all their deposits from Deposit Insurance and Credit Guarantee Corporation (a wholly owned subsidiary of RBI) (hereinafter referred to as 'DICGC').

Banks take this insurance for all kinds of Deposits viz., Fixed Deposits, Savings, Current etc. Further, they do not charge any amounts on its deposit holders in case of early termination of the deposits, interest that is payable to the deposit holders will be reduced proportionately, and no charge will be levied directly on the deposit holders.

This has led to departmental notices being issued by the service tax department denying the CENVAT credit on the grounds that, such insurance premium paid on the deposits does not qualify as 'input service' in terms of Rule 2(l) of CENVAT Credit Rules, 2004, since 'deposits' fall under negative list of services and since no output service tax is paid by banks on such deposits therefore insurance premium paid on insuring of such deposits shall be directly ineligible to be availed as CENVAT credit.

Eligibility of CENVAT credit - Legislative view

Rule 6(3B) of the CENVAT Credit Rules, a Banking company and a financial institution engaged in providing services by way of extending deposits, loans or advances, in addition to other options given under rule 6(1) (2) and (3) of the CENVAT credit rules, shall have the option to pay every month an amount equal to 50% of the CENVAT credit availed on inputs and input services in that month.

~~Further, for the period prior to 01.04.2016, the above said rule stated that, a Banking company and a financial institution engaged in providing services by way of extending deposits, loans or advances, in addition to other options given under rule 6(1) (2) and (3) of the CENVAT credit rules, shall have the option to~~ pay every month an amount equal to 50% of the CENVAT credit availed on inputs and input services in that month.

This rule was initially introduced in the Budget 2011 and while explaining the budget changes in the year 2011, Tax Research Unit of the CBEC vide para 1.15 of **TRU D.O.F.No.334/3/2011-TRU dated 28th February, 2011** stated that there have been difficulties in ascertaining the amount of credit flowing into earning of the revenue by the banks and financial institutions. **Thus a banking company** or a financial institution, including NBFC, providing banking and financial services **are being obligated to pay an amount equal to 50% of the credit availed.**

Similar view is also clarified in point 11 of Circular No.943/04/2011-CX, wherein it is states that Rule 6(3B) **is an obligation** on the entities providing Banking & Financial Services.

Therefore, till 31.03.2016, it was obligation cast on banking companies to follow the reversal of CENVAT credit @ 50% on all input services without making any bifurcation as to actual. However, from 01.04.2016, Banks have been given option to choose as to whether reversal of CENVAT credit is preferred @ standard rate of 50% under Rule 6(3B) or to opt for reversal on actual basis as per rule 6(1), (2) and (3) of the CENVAT credit rules.

While explaining the budget changes in the year 2016-17, Tax Research Unit of the CBEC vide Annexure II of **TRU D.O.F.No.334/8/2016-TRU dated 29th February, 2016** stated that Sub-rule (3B) of rule 6 is being amended so as to allow banks and other financial institutions to reverse credit in respect of exempted services on actual basis in addition to the option of 50% reversal.

Therefore, it is always a view that banks have to either reverse CENVAT credit either based on actual or standard reversal of 50% must be made based. Each rules was exclusive of each other.

Applying both the rules together was never intended as per the paperwriters and may not have been the intention of the law makers.

Even if it were to be done in such a narrow way, the CENVAT credit would be available in such cases as explained below.

Rule 3(1) read with rule 3(4) of CCR specifies that the provider of taxable services could avail the credit on **eligible** inputs, input services and capital goods received, which could be set off against output service tax liability.

Further as per Rule 6(3B) of CENVAT Credit Rules, 2004, Banking Company and a Financial Institution (including a Non-Banking Financial Company), engaged in providing services by way of extending deposits, loans or advances shall pay for every month an amount equal to 50% of the CENVAT credit availed on inputs and input services in that month.

Definition of input service: Under Rule 2 (I) of CCR, input service means any service,

i. used by a provider of output service for providing an output service,....

ii.;

*and includes **services used in relation to** modernization, renovation or repairs of factory, premises of provider of output service or an office relating to such factory or premises, advertisement or sales promotion, market research, storage upto the place of removal, procurement of inputs, accounting auditing, **financing**, recruitment and quality control, coaching and training, computer networking, credit rating, share registry, security business exhibition,*

legal services, inward transportation of inputs or capital goods and outward transportation upto place of removal but excludes -.....

Since, deposits does not fall within the definition of output service, it becomes relevant to check if the insurance premium paid on such deposits would get covered under the ambit of '**financing**' under the inclusive limb of the definition.

Further, as per the second limb of the definition which starts from the inclusive clause makes it clear that the services covered under the inclusive definition do not require the nexus or connection in relation to providing the output service or manufacture of final products.

The word 'include' is used in interpretation clauses in order to enlarge the meaning of words or phrases occurring in the body of the statute; and when it is so used, these words or phrases must be construed as comprehending, not only such things as they signify according to their natural import but also those things which the interpretation clause declares that they shall include. The scope meant to be construed as 'wide enough and limited in scope'. The clause needs to be interpreted accordingly.

From the Jurisprudence:

The following case laws can be relied on as far as the eligibility of CENVAT credit on the activities covered by inclusive limb of the definition of input services are concerned:

Coca Cola India Pvt. Ltd. v. CCE [2009 (15) S.T.R. 657 (Bom.) it was held that each limb of the definition of input service can be considered as an independent benefit or concession exemption. If an assessee can satisfy any one of the limbs of the above benefit, exemption or concession, then credit of the input service would be available. This would be so even if the assessee does not satisfy other limb/limbs of the above definition. To illustrate, input services used in relation to setting up, modernization, renovation or repairs of a factory will be allowed as credit, even if they are assumed as not an activity relating to business as long as they are associated directly or indirectly in relation to manufacture of final products and transportation of final products upto the place of removal.

Aditya Birla Nuvo Ltd. Vs. Commissioner of central Excise, Bhavnagar 2009 (14) S.T.R. 304 (Tri. - Ahmd.) "The definition of input service has been expanded by using the words "and includes" basically for the reason that the services which are enumerated after the words "and

includes” are those services which may not be considered as directly or indirectly relatable to manufacture but yet the intention is to provide the benefit of credit of service tax paid on such services as CENVAT credit. Therefore what is required to be examined is whether the services on which credit has been denied can be covered by the categories of services listed in the definition.

Further, in the case of **Commissioner of Central excise Vs Fiamm Minda Automotive Ltd. 2016 (43) S.T.R 549 (Tri.- Del)** it was held that Banking and other financial services are covered in the inclusive part of definition of input service under the head “financing” - said services have been used/utilised for accomplishing manufacturer/service provider in terms of Rule 2(I) of Cenvat Credit Rules, 2004.

Based on the above cases, it can be inferred that **‘Financing’** is specifically covered in the second limb of the definition and thus satisfies the definition of input services.

Similar judicial views

In the Case of **Bank of Baroda Ltd. Vs Commissioner of Central Excise 2015(37) S.T.R 488 (Tri-Mumbai)** it was held that brokerage for sale/purchase of shares and securities for trading, custodian charges, paid by the banking company are statutory expenses to be incurred by the applicant to do their banking business and therefore they are in the nature of input services having nexus to their business activity.

In the case of **Stock Holding Corporation of India Ltd Vs Commissioner of Service tax, 2015 (39) S.T.R. 664 (Tri-Mum)** it was held that Insurance service is availed for insuring the business risk, therefore allowable as input service.

In case of **Bank of India Vs Commissioner of CE & ST (Indore) 2015 (38) S.T.R. 982 (Tri. - Del.)**, it was held that hiring of security vans and rent-a-cab services etc. are required for cash management and are used for providing Banking and Financial services and therefore falls within the ambit of input services.

Conclusion:

Firstly, the intent of legislature is clear that once 50% of CENVAT credit is reversed by the banking companies then again CENVAT credit need not be reversed on actual one-to-one

nexus basis. However, even otherwise it is to be noted that although deposits are covered under negative list, but for banks the activity of accepting deposits is in the nature of receipt of service for which banks would require to pay an interest to the deposit holder. Such deposits are like an activity of **'financing'** for banks which is specifically covered as input service as per rule 2(l) of CENVAT credit rules.

Output services of the Banks are in the nature of lending, advancing, providing overdrafts etc. on which banks are paying service tax. Such output services of lending, advancing etc. cannot be provided by banks if they do not create 'financing' in the form of accepting deposits. Therefore, insurance premium is paid on deposits only to safeguard its finances and therefore there is a complete nexus and insurance premium paid for insuring of deposits qualify as an eligible input service for availing CENVAT credit. However, until the issue attains finality, departmental officers would take this as another opportunity to harass banking companies vide issuing high value demand notices.

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