

# Corporate guarantee provided by parent company to its subsidiaries without consideration not leviable to service tax - SC

5 April 2023



## Summary

In a landmark judgment, the Supreme Court (SC) has held that service tax is not leviable on the corporate guarantee provided by the assessee to its group companies without consideration. The SC stated that consideration is a must for levying service tax on a corporate guarantee, and thereby, upheld the Customs, Excise and Service Tax Appellate Tribunal's (CESTAT) order.

### Facts of the case

- M/s Edelweiss Financial Services Limited (the assessee) issued a corporate guarantee on the behalf of its group company located within and outside India without any consideration.
- The Revenue contended that the assessee has not discharged the service tax liability on corporate guarantee as the provider of 'banking and other financial services' for the period prior to, and after, 30 June 2012, and issued a show cause notice.
- The adjudicating authority had concluded that the receipt of commission from overseas companies, being consideration for the export of services, was not taxable, and that, insofar as domestic facilitation was concerned, the definition in Section 65(12) of Finance Act, 1994, did not extend to a 'corporate guarantee' which, unlike a 'bank guarantee', finds no specific enumeration as 'other financial services' therein till 20 June 2012. For the period thereafter, the absence of 'consideration' for facilitating a 'corporate guarantee' excluded such activity from coverage within the definition of 'service' in Section 65B(44) of the Finance Act, 1994.
- The CESTAT held that for the purpose of taxability under the Finance Act, 1994, any activity must not only in relation to another, reveal a 'provider', but also the flow of 'consideration' for rendering of the service. In the absence of any of these two elements, taxability under Section 66B of the Finance Act, 1994, will not arise. Thus, there is no consideration insofar as a 'corporate guarantee' issued by the

assessee on behalf of its subsidiary companies is concerned. Therefore, the CESTAT dismissed the Revenue's appeal due to absence of consideration.

- Aggrieved by the CESTAT's decision, the Revenue has filed a civil appeal before the SC.

### SC observations and ruling [Civil Appeal Diary No(s).5258/2023 order dated 17 March 2023]:

- **No evidence to demonstrate taxability:** The SC observed that this was a case where the assessee had not received any consideration while providing a corporate guarantee to its group companies. Further, no effort was made on behalf of the Revenue to assail the above finding or to demonstrate that the issuance of a corporate guarantee to group companies without consideration would be a taxable service.
- **Service tax cannot be levied in absence of consideration:** Since there was no consideration flowing to the assessee, the SC held that in the absence of consideration, no service tax liability emerges.
- **No reason to admit the appeal:** In view of the conclusive finding by the CESTAT and the Commissioner, the SC found no reason to admit this case on the ground that it should be tagged with other pending civil appeals in the case of DLF Cyber City Developers Ltd., as it has not been demonstrated that the factual matrix of both cases is identical.

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## Our comments

This is a significant ruling that will set a precedence in similar matters and help resolve long-drawn litigations on the issue under the erstwhile service tax regime.

Under the GST regime, related party transactions, even without consideration, are treated as deemed supplies and are leviable to GST. In this regard, it is pertinent to note that while the SC has ruled that consideration is a must to levy tax on a corporate guarantee, this may create problems for the businesses under the GST regime. Therefore, the decision is likely to open Pandora's box in cases of corporate guarantees provided by related parties, inter-company, or directors, as more assessees are likely to come under the Revenue's scanner.

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