

AUTHORITY FOR ADVANCE RULINGS
(CENTRAL EXCISE, CUSTOMS AND SERVICE TAX)
NEW DELHI

The 13th May, 2011

Ruling No. AAR /ST/06/2011

In

Application No. AAR/ ST /44/13/2010

Applicant : M/s MAS-GMR Aerospace Engineering Company Ltd,
GMR HIAL Airport Office, Rajiv Gandhi International Airport, Shamshabad,
Hyderabad 500 409

Commissioner Concerned : The Commissioner of Central Excise and Customs,
Hyderabad-IV Commissionerate,
Posnett Bhavan, Tilak Road, Ramkote,
Hyderabad- 500 001

Present for the Applicant : Shri Vikram S.Nankani, Advocate
Shri Tarun Gulati, Advocate
Shri Kishore Kunal, Advocate

Present for the Commissioner : Shri S.N.Singh, Jt. CDR
Shri Sonal Bajaj, SDR

RULING
(By J.K.Batra)

MAS-GMR Aerospace Engineering Company Ltd, the applicant is a joint venture company of GMR, Hyderabad International Airport Limited, Hyderabad and Malaysian Aerospace Engineering, SDN-BHD, Malaysia. The applicant has obtained a registration as a co-developer of an aviation specific SEZ adjacent to the Hyderabad Airport. The applicant either through itself or its 100% subsidiary or by a Special Purpose Vehicle (SPV) has proposed to set up a unit within the SEZ. The applicant has proposed to provide maintenance, repair and overhauling (MRO) facilities to domestic as well as foreign aviation entities. The applicant proposes to enter into a contract with

an overseas entity located in Singapore who will procure contracts for MRO services from domestic and foreign airlines. The overseas entity will sub-contract to the applicant the contract for MRO services which will be carried out in the SEZ. The applicant will be paid in convertible foreign exchange by the overseas entity. The applicant also proposes to enter into direct contracts with domestic and foreign airlines who will pay the applicant in convertible foreign exchange.

2. The applicant proposes to carry out the entirety of the MRO services within the SEZ. According to the applicant the activity of repair gets concluded when the repair is carried out on the aircraft. Therefore, the service is received by the recipients as soon as the repair activity is carried out inside the SEZ. The consumption of the service is also therefore simultaneous.

The applicant has requested for a definitive ruling on the following questions:-

- (1) Whether service tax is applicable on the services rendered by the applicant to the overseas entity for contract with:-
 - (a) Domestic airlines who operate domestic flights to India;
 - (b) Domestic airlines who operate international flights; and
 - (c) Foreign entities who operate international flights.
- (2) Whether service tax is applicable on the services rendered by the applicant directly to:
 - (a) Domestic airlines who operate domestic flights to India;
 - (b) Domestic airlines who operate international flights; and
 - (c) Foreign entities who operate international flights.
- (3) Whether in view of the provisions relating to Sections 51 and 53 of the SEZ Act, 2005, service tax will not be chargeable on the services rendered within the SEZ?
- (4) Whether MRO services proposed to be carried on by the applicant will be chargeable to service tax on an interpretation of Section 66A of the Finance Act, 1994 read with Rule 3(ii) of the Import of Service Rules
- (5) Whether MRO services rendered to the overseas entity for:
 - (a) Domestic airlines who operate domestic flights to India;

- (b) Domestic airlines who operate international flights; and
- (c) Foreign entities who operate international flights.

will qualify as export of services under the Export of Service Rules, 2005?

3.1 Section 53(1) of the Special Economic Zones Act, 2005, by way of deeming fiction, regards an SEZ to be a territory outside the Customs territory of India for the purposes of undertaking authorized operations in the SEZ. Further, section 51 of the SEZ Act provides that the provisions of SEZ will have effect notwithstanding anything inconsistent therewith in any other law. Therefore, it is the applicant's contention that the provisions of the SEZ Act have an overriding effect and will prevail over any other provision which may be inconsistent with the provisions of the SEZ Act. The applicant submits that since SEZ is to be regarded as a territory outside the customs territory of India for the purpose of authorized operations, all laws including Chapter V of the Finance Act, 1994 relating to service tax will not apply to activities in relation to authorized operations carried out within the territory of the SEZ. The MRO services proposed to be carried out in the SEZ are part of the authorized operations of the SEZ. Therefore, according to the applicant service tax will not be applicable on the MRO services to be provided by the applicant and received within the SEZ which is deemed to be a territory outside India.

3.2 It has been argued by the applicant that the deeming fiction created by Section 53 (1) of SEZ Act has to be given its full effect and it has to be interpreted in a manner that benefits the SEZ and thus service tax is not applicable to the activities carried out by the applicant inside the SEZ. Moreover, since the entire activity is carried out inside the SEZ itself, it has no territorial nexus with the DTA where the Finance Act is applicable. In the absence of any territorial nexus, the activity of the applicant, it has been claimed, is not exigible to service tax.

3.3 The applicant further contends that even though the provisions of Finance Act, 1994 apply to the entirety of India except Jammu and Kashmir, in view of the deeming fiction created under Section 53(1) of the SEZ Act, the said Finance Act will not apply to services rendered in the SEZ unless there is specific provision in the SEZ Act itself permitting levy of service tax on services rendered in the SEZ. The applicant has

referred to the following provisions of the SEZ Act to suggest that SEZ territory is deemed to be a territory outside India for the purposes of fiscal levies –

(a) “domestic tariff” area has been defined to mean the whole of India but excluding the areas of SEZ [clause (i) of Section 2]

(b) sale of goods by a unit in SEZ to DTA is considered as import of goods into India [clause (o) of Section 2]

(This is however, factually incorrect, because the said clause (o) does not refer to movement of goods from DTA to SEZ or vice versa)

(c) sale of goods to unit in SEZ is considered as export of goods outside of India. [clause (m) of Section 2].

(d) rule 31 of the Special Economic Zones Rules, 2006 provides exemption from payment of service tax on all taxable services rendered to a developer or a unit by any service provider for the authorized operations in the SEZ.

(e) rule 53 (k) of the SEZ Rules suggests that export of services for a unit includes the services rendered within the SEZ or services rendered to the DTA for which payment is received in foreign exchange. Therefore the SEZ legislation itself grants an implied recognition of “export” to services which are provided by the SEZ unit.

The applicant claims that the aforesaid provisions confirm that SEZ territory is deemed to be a territory outside India for the purpose of fiscal levies.

3.4 Further neither the Finance Act, 1994 nor the SEZ Act expressly provide for levy of service tax on the activities carried out and consumed inside the SEZ. Section 27 of the SEZ Act provides for application of Income Tax Act, 1961 to a unit or developer for carrying out the authorized operations in a SEZ with modifications specified therein; there is no provision in the SEZ Act making the Chapter V of the Finance Act relating to service tax applicable to SEZs with or without modification. Further in the case of goods a specific provision (Section 30) has been made providing for levy of Customs duty on goods cleared to the DTA from SEZ, however, no similar provisions exist for services.

4.1 Accordingly to the applicant the MRO activities proposed to be undertaken by it are covered by the taxing entity of “management, maintenance and repair services” as

under clauses (64) & (105) (zzg) of Section 2 of the Finance Act, 1994. However, the liability to service tax will arise only if such services satisfy the test of territorial nexus and whether such services fall within the ambit of charge created under Section 66A of the Finance Act read with the exemption provided under the Import of Service Rules [that is, the Taxation of Services (Provided from Outside India and Received in India) Rules, 2006]. The applicant submits that since the performance of the service is in a SEZ which is wholly outside India, the service will not be regarded as import of services in India in terms of Rule 3 (ii) of the Import of Service Rules. Consequently no service tax is leviable on MRO services proposed to be rendered by the applicant to foreign and domestic airlines within the territory of SEZ. As per the applicant this position will apply both for contracts undertaken on behalf of overseas entity as well as those undertaken directly for foreign or domestic airlines.

4.2 Similarly the applicant has contended that under the Export of Services Rules, 2005 MRO services rendered by the applicant and classifiable under clause (105) (zzg) of Section 65 are specified under rule 3 (1) (ii) of the Rules. They would qualify as export of services if the services are partly or wholly performed outside India and if the payment for said services is received in convertible foreign exchange. Since the services in the case of applicant are performed within the territory of SEZ, it has been claimed to have been performed outside India. Since the payment would be received in foreign exchange, the applicant claims that this service would qualify as export of service in terms of Rule 4 of the Export of Service Rules, 2005 and be exempt from payment of service tax.

5.1 The Commissioner of Central Excise and Customs, Hyderabad-IV, the concerned Commissioner has contested the submissions made by the applicant regarding levy of service tax on the MRO activities proposed to be carried out by the applicant in the SEZ. Citing the statement of objects and reasons while introducing the relevant bill for the SEZ Act, the Commissioner has pointed out that the aims and objects of setting up the SEZs is to promote export led growth. The exemption from duties and taxes on goods and services is only for the purposes of export. The Commissioner has further observed that the exemption from service tax under clause

(e) of Section 26 (1) of the SEZ Act is intended for taxable services provided to a developer or a unit to carry on authorized operations in a Special Economic Zone. Consequently Central Government has notified the exemption from the levy of service tax in such cases in terms of Notification No. 9/2009-ST dated 03.03.2009.

5.2 According to the Commissioner, provisions of Chapter V of the Finance Act, 1994 relating to levy and collection of service tax are applicable to whole of India including the SEZs but excluding the State of Jammu and Kashmir. The Commissioner has cited the judgment of Gujarat High Court in the case of Essar Steels Vs Union of India to support the contention that SEZs form a part of India and cannot be considered as areas outside India. He has referred to similar observations of the High Court of Karnataka in the case of Shyamraju and Co (India) Pvt. Ltd., Vs Union of India wherein the Court has observed that “if a SEZ was to be treated as being outside India there was hardly any necessity under Section 26 to exempt from Customs duty any goods which are imported into a SEZ.....”

5.3 The MRO services falling under the category of Section 65 (105) (zzg) of the Finance Act, 1994 to be provided by the applicant within the SEZ are not for the authorized operations of SEZ and will be provided to various Indian and foreign customers. Hence the MRO services to be provided by the applicant within the SEZs are to be treated as services provided within the territory of India and are leviable to service tax under Section 66 of the Finance Act.

5.4 Further, in terms of Section 66A read with Rule 3 (ii) of Taxation of Services (Provided from Outside India and Received in India) Rules, 2006 maintenance or repair services should be performed partly or wholly within India to attract the charges of Service Tax. Since in the case of the applicant the entire MRO services will be rendered within the SEZs in India, these are to be treated as services provided within India and hence the applicant is liable to pay service tax.

5.5 The Commissioner, further contends that in terms of rule 3 (1) (ii) of Export of Service Rules, 2005, MRO services will qualify as export if such services are performed partly or wholly outside India. Since in the case of the applicant the MRO services will be performed within the SEZ i.e. within India, such services do not qualify as export as contemplated under Rule 3(i) (ii) aforesaid.

6.1 During the course of the arguments also the Departmental Representatives questioned the assumption of the applicant about the non application of the service tax laws to the SEZs. It was pointed out that the contention of the applicant that the Finance Act, 1994 does not apply to SEZ, if accepted, would result in absurd situations. Firstly the application for advance ruling itself would be beyond the jurisdiction of the Authority. Further, while sub-section (1) of Section 53 of the SEZ Act would deem a SEZ to be a territory outside India, sub-section (2) of the said Section 53 designates a SEZ to be a port, airport, ICD etc., in India under the provisions of Customs Act, 1962. Moreover, if the SEZs are to be treated as territories lying outside India, there is no need for the SEZ Act, 2005 to be specifying the exemptions under Section 26. The DR submitted that a deeming fiction should be restricted to the Section which creates it and it cannot be extended beyond the purpose for which it has been created. The DR cited various judgments of the Hon'ble Supreme Court to support his view.

6.2 It was further contended on behalf of the Department that unless there is a specific provision to grant an exemption to activities undertaken in a unit in SEZ, either by the SEZ Act or by any other Act or through an exemption issued under any specific act, the activities are taxable.

7.1 The issues raised by the applicant in its application before the Authority relate to levy of service tax on maintenance, repair and overhaul services proposed to be rendered by the applicant in a unit located in a Special Economic Zone. The applicant has further sought a ruling specifically to the applicability of service tax if the services are rendered directly to the airlines or through an overseas entity. It has also desired to know whether the MRO services rendered to the overseas entity will qualify as export of services. The text of questions on which the ruling has been sought have been set out in paragraph 2.

7.2 The applicant has almost entirely based its interpretation of law in respect of the questions raised for advance ruling on the argument that in terms of Section 53 of the SEZ Act an SEZ is a territory outside India and the Finance Act, 1994 providing for levy and collection of the service tax has no applicability to the operations carried out within

the SEZ. The applicant has also relied on Section 51 of the SEZ Act in an attempt to suggest that the provisions of the SEZ Act will prevail over any other enactment.

Sub-section (1) of Section 53 reads as follows:

“A Special Economic Zone shall, on and from the appointed day, be deemed to be a territory outside the customs territory of India for the purposes of undertaking the authorized operations.”

Provision Section 51 of the SEZ Act are set out below:-

“ The provisions of this Act shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force or in any instrument having effect by virtue of any law other than this Act.”

7.3 The applicant has contended that a combined reading of the aforesaid two provisions implies that an SEZ is deemed to be a territory outside India and in view of the supremacy of the SEZ Act under Section 51, the Finance Act, 1994 shall have no application to operations undertaken in an SEZ. Consequently there is no basis for levy of service tax on services provided in a deemed foreign territory. The applicant has also relied upon Section 27 of the SEZ Act regarding applicability of Income Tax laws as also certain definitions in the SEZ Act to justify its contention.

7.4 As is observed sub-section (1) of Section 53 provides that a Special Economic Zone shall be deemed to be a territory outside **the Customs territory** of India for the purposes of **undertaking the authorized operations**.(Emphasis supplied). The applicant has omitted to take into consideration, presumably by oversight, the term “Customs” in the phrase “Customs territory of India” for defining the territorial status of a Special Economic Zone. The applicant has also overlooked the fact that the deeming fiction has been created for the specific purpose of undertaking the authorized operations as defined in the SEZ Act. “Customs territory” is a well known term in international trade parlance and has been defined in the United Nations International Trade Statistics Knowledgebase as *“the territory in which the customs law of a state applies in full”*. A similar definition of “Customs Territory” has been provided in the International Convention on the Simplification and Harmonization of Customs Procedures (Kyoto Convention), an instrument finalized under the auspices of the World

Customs Organization (WCO). Customs territory has been defined therein to mean “*the territory in which the Customs law of a Contracting Party applies*”. Effectively sub-section (1) of Section 53 of SEZ Act is a policy declaration by a deeming fiction that the authorized operations undertaken in areas notified as Special Economic Zones under the SEZ Act shall be beyond the customs laws of the country. It does not state nor can it be inferred or implied that the area notified as an SEZ under the SEZ Act lies physically outside India as defined in the Constitution of India or that any law declared by Parliament to apply to whole of India shall not have effect in an SEZ. The provisions of sub-section (1) of Section 53 have apparently been misconstrued by the applicant by ignoring the usage of the word “Customs” in the phrase “Customs territory of India” in the sub-section.

7.5 Without delving too much into the SEZ scheme, even a cursory glance at some of the provisions of the SEZ Act and the Rules thereunder would reveal that the interpretation sought to be advanced by the applicant is entirely misplaced. Rule 25 of the Special Economic Zones Rules, 2006 reads as follows:-

*“ Where an entrepreneur or Developer does not utilize the goods or services on which exemptions, drawbacks, cess and concessions have been availed for the authorized operations or unable to duly account for the same, the entrepreneur or the Developer, as the case may be, shall refund an amount equal to the benefit of exemptions, drawback, cess and concessions availed **without prejudice to any other action under the relevant provisions of the Customs Act, 1962, the Customs Tariff Act, 1975, the Central Excise Act, 1944, the Central Excise Tariff Act, 1985, the Central Sales Tax Act, 1956, the Foreign Trade (Development and Regulation) Act, 1992 and the Finance Act, 1994(in respect of service tax) and the enactments specified in the First Schedule to the Act, as the case may be**”*

7.6 Accordingly where the exempted goods/services entered into a SEZ are not utilized for authorized operations or are not duly accounted for, penal action can be taken against the entrepreneur or developer *inter alia* under the Customs Act, 1962 and other Customs Laws. In other words, Customs laws have been made applicable to SEZs in the SEZ scheme itself under specific situations. This provision complements the provisions of sub-section (1) of Section 53 of the SEZ Act and is a confirmation that

SEZs have been declared as being outside the Customs territory of India for a specified purpose only that is, undertaking authorized operations.

7.7 A reference is also invited to Section 26 of the SEZ Act which lists out the exemptions from Customs and Excise duties for goods moving in and out of SEZ. If an SEZ were really deemed to be a territory outside India as the applicant would like us to believe there was apparently no need for such an expansive list of exemptions & concessions. Infact there was no need to exempt goods from customs and excise duties under Indian laws when such goods are intended to be supplied to foreign lands. Likewise there was no need for granting exemptions under Section 7 of the SEZ Act from payment of taxes, duties or cesses under 21 different fiscal statues listed in the First Schedule to the Act if SEZs were to be deemed to be territories outside India. We are inclined to agree with the Department that the interpretation sought to be placed by the applicant would lead to “contradictions & absurd situations” and therefore is not acceptable. Consequently all enactments (whether relating to fiscal levies, labour laws, banking laws or any other law) which apply to the territory of India apply in equal measure to the notified areas of special economic zones as well. If a particular law is applied to SEZs with modifications (the Income Tax Act,1961 applied to SEZ under Section 27 of the SEZ Act), it cannot lead to an inference that other laws which may not have been specifically mentioned in the SEZ Act have no application to SEZs All central laws apply to SEZs with modifications or exceptions, if any, as provided in the SEZ Act itself or in rules made thereunder.

7.8 Provision of Section 51 of the SEZ Act relating to the said Act having an overriding effect would need to be invoked only if any inconsistency is noticed between the provisions of the SEZ Act and any other law for the time being in force. The question before us pertains to the applicability of the Finance Act, 1994 providing for levy of service tax in respect of operations carried out by a unit in a SEZ. Section 64 of the said Finance Act provides that Chapter V of the said Act extends to the whole of India except the State of Jammu and Kashmir. Services provided to and from an entity in a SEZ are provided from India. Section 53(1) of the SEZ Act does not make the Finance Act, 1994 inapplicable to a SEZ. In the absence of any inconsistency there is no need to invoke section 51 of the SEZ Act.

7.9 Section 66 A of the Finance Act, 1994 provides for levy of service tax under certain specified situations on services received from outside India. The applicant has claimed that since the MRO services are provided in a SEZ which according to him is outside India no such tax is leviable under the said provision. However, as discussed in the preceding paragraphs SEZs are deemed to be outside the customs territory of India only for undertaking authorized operations; all other enactments are applicable to the operations carried out in the SEZs. The MRO services would therefore be performed within the territory of India and Section 66 A will have no application in the context of these activities. The services provided by the applicant would be taxable under Section 66 of the said Finance Act, 1994.

7.10 The aforesaid MRO services provided by the applicant cannot also be considered as export of taxable services under the Export of Services Rules, 2005 since in terms of clause (ii) of Rule 3 (1) of the Export of Services Rules, services specified in sub-clause (zzg) of clause (105) of Section 65 of the Finance Act shall be considered as export only if such services are performed outside India. SEZs being part of India, performance of such services in the SEZs does not entitle them to be categorized as exports of taxable services.

8. Questions raised by the applicant are accordingly answered as follows:-

Question No.1

Whether service tax is applicable on the services rendered by the applicant to the overseas entity for contract with:-

- (a) Domestic airlines who operate domestic flights to India;
- (b) Domestic airlines who operate international flights; and
- (c) Foreign entities who operate international flights?

Answer: Yes

Question No.2

Whether service tax is applicable on the services rendered by the applicant directly to:

- (a) Domestic airlines who operate domestic flights to India;

- (b) Domestic airlines who operate international flights; and
- (c) Foreign entities who operate international flights?

Answer: Yes

Question No. 3.

Whether in view of the provisions relating to Sections 51 and 53 of the SEZ Act, 2005, service tax will not be chargeable on the services rendered within the SEZ?

Answer: Service tax will be chargeable on the services rendered within the SEZ unless specifically exempted under the SEZ Act or under the Finance Act, 1994 or any Rules or Notifications there under. There is no such exemption presently available in respect of MRO services proposed to be provided by the applicant.

Question No. 4

Whether MRO services proposed to be carried on by the applicant will be chargeable to service tax on an interpretation of Section 66A of the Finance Act, 1994 read with Rule 3(ii) of the Import of Service Rules

Answer: Yes

Question No.5

Whether MRO services rendered to the overseas entity for:

- (a) Domestic airlines who operate domestic flights to India;
- (b) Domestic airlines who operate international flights; and
- (c) Foreign entities who operate international flights.

will qualify as export of services under the Export of Service Rules,2005?

Answer: No

Accordingly Ruling is given and pronounced on this day, the 13th of May, 2011.

Sd/-
(J.K.Batra)
Member

Sd/-
(P.K.Balasubramanyan)
Chairman

Sd/-
(J.Khosla)
Member

