

**CUSTOMS, EXCISE AND SERVICE TAX APPELLATE TRIBUNAL
CHENNAI**

REGIONAL BENCH – COURT No. III

Service Tax Appeal No. 40038 of 2020

(Arising out of Order-in-Original No. 66/Commr./ST/2019 dated 30.09.2019 passed by Commissioner of GST and Central Excise, No. 1, Williams Road, Cantonment, Tiruchirappalli – 620 001)

M/s. Karur Vysya Bank Ltd.

Finance and Control Department,
Central Office, Erode Road,
Karur – 639 002.

...Appellant

Versus

Commissioner of GST and Central Excise

Tiruchirappalli Commissionerate,
No. 1, Williams Road,
Cantonment,
Trichy – 620 001.

...Respondent

And

Service Tax Appeal No. 40247 of 2020

(Arising out of Order-in-Original No. 01/Commr./ST/2020 dated 31.01.2020 passed by Commissioner of GST and Central Excise, No. 1, Williams Road, Cantonment, Tiruchirappalli – 620 001)

M/s. City Union Bank Ltd.

24-B, Gandhi Nagar,
Kumbakonam – 612 001.

...Appellant

Versus

Commissioner of GST and Central Excise

Tiruchirappalli Commissionerate,
No. 1, Williams Road,
Cantonment,
Trichy – 620 001.

...Respondent

APPEARANCE:

For the Appellants : Mr. S. Ananthan, Chartered Accountant

For the Respondent : Ms. Anandalakshmi Ganeshram, Authorised Representative

CORAM:

HON'BLE MR. P. DINESHA, MEMBER (JUDICIAL)

HON'BLE MR. VASA SESHAGIRI RAO, MEMBER (TECHNICAL)

FINAL ORDER Nos. 40135-40136 / 2026

DATE OF HEARING : 20.08.2025

DATE OF DECISION : 22.01.2026

Per Mr. VASA SESHAGIRI RAO

The Appellants, M/s. City Union Bank Limited (CUB) and M/s. Karur Vysya Bank Limited (KVB), are scheduled banking companies engaged in providing Banking and Other Financial Services to customers across India. Both Banks were holding centralised Service Tax registrations during the relevant periods and were regularly filing ST-3 returns, discharging service tax wherever applicable, and availing CENVAT credit in accordance with the law.

1.2 Both the Banks were subjected to periodic departmental audits, and their books of accounts and statutory records were made available to the Department during the course of such audits.

2. The period involved in the appeal filed by City Union Bank Limited is 01.04.2014 to 30.06.2017.

2.1 During verification of the financial records of the Bank, the Department noticed the following: -

- i. the Bank had collected penal interest from borrowers on account of delay or default in payment of EMIs in respect of term loans; and
- ii. the Bank had incurred expenditure under Corporate Social Responsibility (CSR) and allied activities, which according to the Department involved sponsorship

services, attracting service tax under Reverse Charge Mechanism (RCM).

2.2 The Department took the view that penal interest collected by the Bank constituted consideration for "tolerating an act", taxable as a declared service under Section 66E(e) of the Finance Act, 1994.

2.3 In respect of CSR expenditure, it was alleged that wherever such expenditure involved display of the Bank's logo, name or brand visibility, or where documentation evidencing pure donation was allegedly insufficient, the activity amounted to "sponsorship service" as defined under Section 65(99a) of the Act.

2.4 Accordingly, a Show Cause Notice 35/COMMR/ST/2019 dated 15.10.2019 was issued proposing to demand: Service Tax of ₹6,45,91,501/- on penal interest; Service Tax of ₹3,90,56,551/- plus ₹98,686/- under RCM on CSR/sponsorship expenditure; and Interest under Section 75; and Penalties under Sections 77 and 78, by invoking the extended period of limitation under the proviso to Section 73(1) of the Finance Act, 1994.

2.5 *Vide* the impugned Order-in-Original 01/COMMR/ST/2020 dated 31.01.2020, the Commissioner of Central Excise, Trichy confirmed the demand of service tax of Rs 5,67,61,006/- on penal interest and demand under RCM of Rs 1,99,01,781/- & Rs 98,686/- on CSR/sponsorship expenditure; appropriated minor amounts already paid; and imposed penalties under Sections 77 and 78 of the Finance Act, 1994.

2.6 Aggrieved by the said order, City Union Bank Limited has preferred the present appeal before this Tribunal.

3. The period involved in the appeal filed by Karur Vysya Bank Limited is October 2013 to June 2017.

3.1 During audit and verification of records, the Department observed that:

- i. the Bank had collected penal interest from borrowers on delayed payment of EMIs;
- ii. the Bank had recovered liquidated damages / notice period pay from employees who resigned without serving the stipulated notice period; and
- iii. the Bank had incurred CSR expenditure, part of which allegedly constituted sponsorship services attracting tax under RCM.

3.2 The Department alleged that both penal interest and liquidated damages were taxable as consideration for tolerating an act under Section 66E(e).

3.3 In respect of CSR expenditure, it was alleged that wherever there was reciprocity, brand visibility or lack of adequate documentation, the same was liable to tax as sponsorship service under Section 65(99a) read with RCM provisions.

3.4 Accordingly, a Show Cause Notice No 02//COMMR/ST/2019 dated 15.04.2019 was issued proposing demand of: Service Tax of ₹18,28,78,097/- on penal interest; Service Tax of ₹31,50,236/- on liquidated damages / notice period pay; Service Tax of ₹74,77,344/- under RCM on sponsorship services; Interest under Section 75; and Penalties under Sections 77 and 78, by invoking the extended period.

3.6 *Vide* the impugned Order-in-Original No 66/COMMR/ST/2019 dated 30.09.2019, the Commissioner of Central Excise, Trichy: -

- i. dropped demand to a limited extent;
- ii. appropriated certain amounts already paid by the Bank; and

iii. confirmed the following demands of ₹16,11,07,260/- towards penal interest; ₹27,68,700/- towards liquidated damages; ₹55,59,981/- towards sponsorship services under RCM; along with Interest under Section 75; and imposed penalties under Section 78.

3.7 Aggrieved by the confirmation of the above demands, Karur Vysya Bank Limited has filed the present appeal.

4. Since both appeals ST/40247/2020 and ST/40038/2020 raise identical questions of law on: i) taxability of penal interest; ii) taxability of liquidated damages / notice pay; iii) taxability of CSR expenditure under sponsorship service; iv) invocation of extended period; and v) sustainability of penalties, the appeals are taken up for disposal by this common order.

4. The Ld. Chartered Accountant Mr. S. Ananthan, appeared on behalf of the Appellants and advanced detailed submissions in support of the Appeals and the Ld. Authorized Representative Ms. Anandalakshmi Ganeshram, appeared for the Revenue and defended the Impugned Orders.

5. The Ld. Chartered Accountant Mr. S. Ananthan has made the following submissions which are summarized as below: -

5.1 The demand on penal interest has been confirmed on the erroneous premise that collection of penal interest amounts to consideration for "tolerating an act" under Section 66E(e) of the Finance Act, 1994.

5.2 That penal interest is levied only upon default or breach of loan repayment terms and is compensatory/deterrent in nature. It is neither a consideration for any independent activity nor a service consciously agreed to be rendered by the Banks.

5.3 The issue is now conclusively settled by the Hon'ble Supreme Court in *Clix Capital Services Pvt. Ltd. v. CST [2024 (8) TMI 98 (SC)]*, affirming the Tribunal's view that penal charges / liquidated damages do not constitute as consideration for tolerating an act and are not exigible to service tax.

5.4 The above position stands reinforced by the decision of the Tribunal in South Eastern Coal Fields Ltd., which has attained finality with the Hon'ble Supreme Court dismissing the Departmental appeal as withdrawn. Numerous

Tribunal decisions including Repco Home Finance Ltd., Bajaj Finance Ltd., Karur Vysya Bank Ltd. have consistently held that penal interest collected by the Banks to be non-taxable.

5.5 Further, CBIC Circular No. 102/21/2019-GST dated 28.06.2019 and Circular No. 178/10/2022-GST dated 03.08.2022 categorically clarify that penal interest and liquidated damages are not liable to tax.

5.6 Accordingly, the demand of service tax on penal interest in both appeals is unsustainable and liable to be set aside.

Notice period pay in respect of M/s. KVB: -

5.7 Notice period pay arises out of an employment contract. Services provided by an employee to an employer are expressly excluded from the scope of service tax under Section 65B (44).

5.8 The Hon'ble Madras High Court in *GE T&D India Ltd. v. Dy. CCE [2020 (1) TMI 1096 (Mad.)]* has held that notice pay recovered from employees is not taxable. The issue also stands covered by South Eastern Coal Fields Ltd., which clarifies that damages for breach of contract are not taxable under Section 66E(e).

5.9 Hence, the demand of service tax on liquidated damages / notice period pay recovered by KVB is liable to be set aside.

CSR Expenditure: -

5.10 The CSR expenditure incurred by the Banks is largely in the nature of pure donations towards social welfare activities such as construction of schools, hospitals, toilets, medical aid, etc., without any quid pro quo.

5.11 Section 65(99a) of the Finance Act, 1994 expressly excludes donations or gifts, provided the Recipient is under no obligation to provide anything in return. Sponsorship pre-supposes the existence of an event and a reciprocal commercial benefit such as branding, logo display linked to an event, or exclusive rights.

5.12 In several instances, the impugned Orders proceeded merely on assumptions of visibility or goodwill, without establishing the existence of an identifiable event or reciprocity, and in some cases travelled beyond the scope of the Show Cause Notices by invoking an "advertisement" theory.

5.13 The Banks have already discharged service tax under RCM on admitted sponsorship activities, and the same

is not in dispute. The remaining demands on CSR expenditure are unsustainable.

5.14 The Banks are regulated entities, regularly filing returns and subjected to departmental audits. The issues involved are purely interpretational and were subject to divergent judicial views.

5.15 In the absence of suppression or intent to evade tax, invocation of the extended period of limitation is not sustainable, as held in Padmini Products, Nizam Sugar Factory, Punjab Laminates, and other decisions.

5.16 When the substantive demands fail, interest and penalties under Sections 75, 77 and 78 cannot survive.

5.17 In view of the above submissions, it was humbly prayed that the appeals be allowed with consequential relief.

6. The Ld. Authorized Representative Ms. Anandalakshmi Ganeshram submitted as follows: -

6.1 That the Learned Adjudicating Authorities have correctly held that penal interest collected from customers and liquidated damages / notice period pay collected from employees are taxable as declared services under Section

66E(e) of the Finance Act, 1994, being consideration for tolerating an act, namely delay or breach of contractual obligations.

6.2 The findings recorded in the Orders-in-Original clearly bring out that the Banks, by levying such charges, consciously tolerate the delay/default in repayment of EMIs or shortfall in notice period, in lieu of monetary consideration.

6.3 That reliance is placed on the detailed discussion contained in the impugned orders (CUB: paras 13–14; KVB: paras 13–14), wherein the nature of these charges and their nexus with Section 66E(e) have been elaborately examined.

6.4 With regard to CSR expenditure, it is submitted that the Revenue does not dispute that pure donations or gifts, where the service provider is under no obligation to provide anything in return, are excluded from the scope of “sponsorship” under Section 65(99a) of the Finance Act, 1994.

6.5 However, on facts, it has been established that in several instances the CSR expenditure incurred by both CUB and KVB involved: display of the Bank’s logo or

company name, conscious insistence on visibility and branding, and absence of adequate documentary evidence to establish that the expenditure is a pure donation.

6.6 Section 65(99a) expressly includes within "sponsorship" the activities of displaying the sponsor's logo or trading name, naming an event, granting exclusive or priority booking rights, or sponsoring prizes or trophies, independent of each other.

6.7 The Ministry's TRU Letter No. 334/4/2006-TRU dated 28.02.2006 clarifies that sponsorship is an alternate form of advertisement, undertaken with an intent to derive commercial benefit, goodwill or brand visibility. The definition does not mandate that naming of an event is a sine qua non; display of logo or branding by itself is sufficient to attract tax.

6.8 The statutory framework governing sponsorship services and reverse charge liability was consistently in force during the relevant periods imposing 100% reverse charge on the service recipient.

6.9 The fundamental principle applicable is "reciprocity" or "quid pro quo". Wherever CSR expenditure

results in branding, visibility, or promotional advantage to the Bank, the activity squarely falls within the ambit of taxable sponsorship service, and service tax is rightly payable under RCM.

6.10 Internal correspondences and records relied upon in the Orders-in-Original demonstrate that both Banks consciously ensured display of their name and logo at places where CSR expenditure was incurred, thereby establishing a clear *quid pro quo*.

6.11 Donations or contributions for which no documentary proof is furnished, or where branding obligations are evident, have therefore been correctly classified as sponsorship services taxable under Section 65(99a) read with Section 65B(44) of the Finance Act, 1994.

6.12 Since the demands have been correctly confirmed on merits, interest under Section 75 follows as a statutory consequence.

6.13 The Banks failed to correctly discharge service tax liability on the above activities and did not properly reflect the same in statutory returns. The Ld. AR has justified invoking the extended period of limitation.

6.14 Penalties under Sections 77 and 78 have been imposed in accordance with law, considering the nature of non-compliance and failure to correctly assess tax liability.

6.15 In view of the foregoing submissions, she has put forth to uphold the impugned Orders-in-Original and reject the appeals filed by the Appellants.

7. We have carefully heard the submissions advanced by both sides, examined the appeal records in detail, considered the statutory provisions, notifications and circulars and the case Laws cited.

8. Upon such comprehensive consideration on the basis of the pleadings, records, and submissions advanced by both sides, the following common questions of law and fact arise for determination in these appeals: -

- i. Whether the penal interest collected by the Appellant Banks from borrowers for delay or default in repayment of EMIs is liable to service tax as a declared service under Section 66E(e) of the Finance Act, 1994, on the ground that the Banks have "tolerated an act"?
- ii. Whether the liquidated damages / notice period pay recovered by Karur Vysya Bank Limited from employees who resigned without serving the stipulated

notice period is liable to service tax under Section 66E(e) of the Finance Act, 1994?

- iii. Whether the CSR expenditure incurred by the Appellant Banks is liable to service tax under Reverse Charge as "sponsorship service" under Section 65(99a) of the Finance Act, 1994, particularly where the Department alleges quid pro quo, brand visibility or insufficient documentation?
- iv. Whether the extended period of limitation under the proviso to Section 73(1) of the Finance Act, 1994 has been validly invoked in the facts and circumstances of the case?
- v. Whether the demands of interest under Section 75 and penalties under Sections 77 and 78 of the Finance Act, 1994 are sustainable?

9. Now, we take up the issues in seriatim.

9.1 Before adverting to the questions framed for determination, it is necessary to first examine the statutory framework governing the levy of service tax on the impugned activities and the clarifications issued by the Board. The scope of service tax during the relevant period is governed by the definitions of "service", "declared service" and "sponsorship service" as contained in the Finance Act, 1994, particularly under Sections 65B (44), 66E(e) and

65(99a). These provisions delineate the essential ingredients required to fasten tax liability, namely, the existence of an activity carried out for consideration, the presence of an enforceable obligation in cases of declared services, and the element of reciprocity or quid pro quo in the case of sponsorship.

Section 65(99a) – “Sponsorship”

(As applicable during the relevant period)

“(99a) ‘sponsorship’ includes naming an event after the sponsor, displaying the sponsor’s company logo or trading name, giving the sponsor exclusive or priority booking rights, sponsoring prizes or trophies for competition; but does not include any financial or other support in the form of donations or gifts, given by the donors subject to the condition that the service provider is under no obligation to provide anything in return to such donors.”

Section 66E(e) – Declared Service

(Introduced w.e.f. 01.07.2012)

*“The following shall constitute declared services, namely:
(e) agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act.”*

Section 65B (44) – “Service”

(Definition of Service – Negative List Regime)

*“(44) ‘service’ means any activity carried out by a person for another for consideration, and includes a declared service, but shall not include—
(a) an activity which constitutes merely,*

a transfer of title in goods or immovable property, by way of sale, gift or in any other manner; or

(i) such transfer, delivery or supply of any goods which is deemed to be a sale within the meaning of clause (29A) of article 366 of the Constitution; or

(ii) a transaction in money or actionable claim;

(b) a provision of service by an employee to the employer in the course of or in relation to his employment;

(c) fees taken in any Court or tribunal established under any law for the time being in force."

Explanation 2 (relevant for banking transactions):

"For the purposes of this clause, 'transaction in money' shall not include any activity relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination, to another form, currency or denomination for which a separate consideration is charged."

Rule 2(1)(d)(vii) of Service Tax Rules, 1994

(RCM Sponsorship Service)

"(vii) in relation to sponsorship service provided to anybody corporate or firm located in India, the body corporate or, as the case may be, the firm who receives such sponsorship service."

Notification No. 30/2012-ST dated 20.06.2012

(Reverse Charge – Sponsorship Service)

In respect of sponsorship services, the entire service tax liability shall be discharged by the service recipient under reverse charge mechanism.

9.2 Equally relevant are the clarificatory Circulars issued by the Central Board of Excise and Customs , which are binding on the Department. The Board, through Circular No. 102/21/2019-GST dated 28.06.2019 and Circular No. 178/10/2022-ST dated 03.08.2022, has explained the true scope of "tolerating an act" and clarified that penal charges, liquidated damages, notice pay and similar recoveries arising out of breach of contract are compensatory in nature and do not, by themselves, constitute as a consideration for a taxable service.

CBEC Circular No. 178/10/2022-ST dated 03.08.2022 Clarifies that: "Tolerating an act" requires independent, conscious agreement, Damages for breach, notice pay, penal interest are not taxable and Employment-related recoveries are outside service tax

9.3 The Board has further clarified that for an activity to be taxable under the category of "tolerating an act", there must exist a separate, conscious and independent agreement to tolerate such act for consideration, and that mere occurrence of breach and consequential recovery cannot be elevated to the status of a taxable service. Likewise, in the context of sponsorship, the statutory exclusion in respect of donations or gifts, where the recipient

is under no obligation to provide anything in return, has been reiterated.

9.4 It is in the above statutory and administrative clarifications that the issues arising in the present appeals are required to be examined and answered.

ISSUE NO. (i) Whether penal interest collected by the Appellant Banks for delayed/defaulted EMIs is taxable as a declared service under Section 66E(e) of the Finance Act, 1994?

10.1 The Appellants submitted that penal interest is levied automatically upon breach of repayment terms and is compensatory in nature. It is not a consideration for any service nor is there any agreement to “tolerate” default. Penal interest retains the character of interest on loans and advances, which are excluded from service tax. Reliance was placed on the judgment of the Hon’ble Supreme Court in *Clix Capital Services Pvt. Ltd. v. CST, 2024 (8) TMI 98 (SC)* wherein it has been categorically held that penal charges / penal interest does not constitute consideration for tolerating an act under Section 66E(e). The Appellants further relied upon *South Eastern Coal Fields Ltd. 2023 (12) TMI 1241 - AT - Service Tax, Repco Home Finance Ltd. 2020 (7) TMI 472 - AT - Service Tax CESTAT Chennai, Bajaj Finance Ltd. 2023(8)TMI 473 CESTAT MUMBAI* , and earlier orders of

this very Bench in Karur Vysya Bank, all holding that such charges are not exigible to service tax. CBIC Circulars dated 28.06.2019 and 03.08.2022 were also relied upon.

10.2 The Department contends that levy of penal interest amounts to toleration of delay in payment by the borrower and therefore squarely falls within the ambit of “declared service” under Section 66E(e). It is argued that the adjudicating authority has correctly interpreted the provision and that penal interest is consideration flowing from the borrower to the bank for tolerating default.

10.3 We have heard the submissions of both the sides and find that

10.3.1 It is not in dispute that penal interest is levied by the Appellant Banks only upon default or delay in repayment of EMIs by borrowers, in terms of the loan agreements.

10.3.2 Penal interest is not a charge levied for any independent activity undertaken by the Banks, but is a contractual consequence of breach, intended to act as a deterrent and to compensate the lender for delayed recovery of funds.

10.3.3 The core issue is whether collection of penal interest can be equated with “tolerating an act” for consideration, as envisaged under Section 66E(e) of the Finance Act, 1994.

10.3.4 We find that for Section 66E(e) to apply, there must exist a conscious, positive and pre-agreed obligation to tolerate an act, refrain from an act, or to do an act, where such toleration itself is the object of the contract.

10.3.5 In loan transactions, the Banks do not agree to tolerate default. On the contrary, default is expressly discouraged, and penal interest is imposed only as a consequence of breach, not as a service willingly rendered.

10.3.6 We find that the issue is no longer res integra in view of the judgment of the Hon’ble Supreme Court in *Clix Capital Services Pvt. Ltd. v. CST [2024 (8) TMI 98 (SC)]*. The Hon’ble Supreme Court has unequivocally held that: -

penal charges or liquidated damages arising out of breach of contract do not constitute consideration for tolerating an act; and
mere occurrence of breach and consequent recovery does not amount to provision of a service under Section 66E(e).

The ratio laid down by the Hon'ble Supreme Court is binding under Article 141 of the Constitution, and all contrary views stand eclipsed.

10.3.7 We also note that the Principal Bench of this Tribunal in *South Eastern Coal Fields Ltd. 2023 (12) TMI 1241 - AT - Service Tax* has taken the same view, which has attained finality upon dismissal of departmental appeals by the Hon'ble Supreme Court.

10.3.8 We find that In the case of *Karur Vysya Bank Ltd. v. CCE, 2017 (8) TMI 1114 (CESTAT Chennai)* and *2018 (8) TMI 702 (CESTAT Chennai)*, involving one of the present Appellants itself, this Tribunal had occasion to examine an identical issue, namely the taxability of penal interest recovered by a banking company under Section 66E(e) of the Finance Act, 1994.

10.3.9 In the aforesaid decisions, the Chennai Bench categorically held that penal interest recovered by banks on delayed payment of EMIs is compensatory in nature and does not constitute consideration for "tolerating an act", and therefore does not amount to a taxable service. It was further held that the provisions of Section 66E(e) are not attracted in such circumstances.

10.3.10 The facts in the present appeals are indistinguishable from those considered in the above decisions, and no contrary decision of any higher judicial forum has been brought to our notice.

10.3.11 Judicial discipline requires us to follow the binding precedents of the coordinate Bench, particularly when the issue pertains to one of the same Appellants and involves identical facts and legal questions. Respectfully following the aforesaid decisions, we hold that the demand of service tax on penal interest is unsustainable.

10.3.12 Based on our findings and respectfully following the binding judgment of the Hon'ble Supreme Court in Clix Capital Services Pvt. Ltd., we hold that penal interest collected by the Appellants is not liable to service tax.

ISSUE NO. (ii) Whether liquidated damages / notice period pay recovered from employees (in the case of Karur Vysya Bank) are taxable under Section 66E(e)?

11.1 The Appellant submitted that notice period pay is recovered due to breach of employment contract and arises within an employer-employee relationship, which is specifically excluded from the definition of "service". Reliance was placed on the judgment of the Hon'ble Madras High

Court in *GE T&D India Ltd., 2020 (1) TMI 1096 Madras High Court* which held that notice pay is not exigible to service tax. Further reliance is placed on *South Eastern Coal Fields Ltd. 2020 (12) TMI 912 – CESTAT New Delhi (LB)* and CBIC Circular dated 03.08.2022 clarifying that liquidated damages are not taxable.

11.2 The Department argued that recovery of notice pay involves toleration of breach of contract and therefore qualifies as declared service under Section 66E(e).

11.3 We have heard both the sides and find that the recovery of notice period pay arises exclusively out of the employer–employee relationship, when an employee resigns without serving the stipulated notice period. Such recovery is compensatory in nature and does not involve any activity carried out by the employer for the employee for consideration.

11.4 Section 65B (44) expressly excludes services provided by an employee to employer in the course of employment.

11.5 We also find that the Madras High Court, in the case of *GE T&D India Ltd. v. Deputy Commissioner of Central*

Excise, 2020(1) TMI 1096-Madras HC has ruled that notice period pay recovered from an employee is not exigible to service tax. This principle aligns with the rationale established in cases like *South Eastern Coalfields Ltd. v. Commissioner of Central Excise and Service Tax, Raipur.*, which determined that damages for breach of contract are not "consideration" for a service.

11.6 The Madras High Court held that notice pay is compensation for the sudden exit of an employee, a contractual mechanism, and not a "consideration" for any service rendered by the employer (such as "tolerating" the early exit).

11.7 The court determined that the employer, by accepting notice pay, is not agreeing to an obligation to "refrain from an act, or to tolerate an act or a situation, or to do an act," as defined under Section 66E(e) of the Finance Act, 1994 (which covered "declared services").

11.8 In *South Eastern Coalfields Ltd. versus Commissioner of Central Excise and Service Tax, Raipur 2020 (12) TMI 912 – CESTAT New Delhi* the Tribunal ruled that liquidated damages, penalties, and forfeited earnest money recovered by SECL for breach of contract are

compensatory and not subject to service tax under Section 66E(e) of the Finance Act, 1994. The Departments appeal against this Order was dismissed by the Supreme Court thereby attaining finality.

The tribunal reasoned that liquidated damages are meant to compensate for losses from an "unintended" contract breach, distinguishing them from payment for a "service". They found no express agreement to tolerate an act in exchange for consideration, which is required for a taxable service under Section 66E(e). Instead, penalty clauses were seen as safeguards rather than an agreement to tolerate or non-performance as a service. The primary intent of SECL's contracts was for the supply of coal, goods, or services, not to establish a service relationship based on penal clauses.

11.9 We therefore hold that liquidated damages / notice period pay recovered by Karur Vysya Bank Ltd. is not liable to service tax under Section 66E(e) of Finance Act 1994.

ISSUE No. (iii) Whether CSR expenditure incurred by the Appellant Banks is liable to service tax as "Sponsorship Service" under Section 65(99a) under Reverse Charge Mechanism?

12.1 The Appellants submitted that CSR expenditure primarily consists of donations for social welfare activities

such as schools, hospitals, toilets, medical aid, and similar causes. Section 65(99a) expressly excludes donations or gifts where there is no obligation to provide anything in return. It is contended that mere logo visibility or goodwill enhancement does not amount to sponsorship of an event. The Appellants also submitted that the adjudicating authority travelled beyond the Show Cause Notice by confirming demand on an "advertisement" theory without establishing sponsorship of any identifiable event.

12.2 The Department argues that wherever logo/name visibility exists or documentation is insufficient to prove donation, a quid pro quo is established. Reliance was placed on TRU letters TRU Letter (D.O.F. No. 334/4/2006-TRU) dated 28.02.2006 and TRU Letter dated 26.02.2010 (D.O.F. No. 334/1/2010-TRU) 26.02.2010 and Notification No. 30/2012-ST to contend that such expenditure amounts to sponsorship taxable under reverse charge.

12.3 Having heard both the sides, we note that Section 65(99a) includes sponsorship involving naming of events, logo display, exclusive rights, etc., but explicitly excludes donations or gifts where the service provider is under no obligation to provide anything in return. TRU Circular Dated 26.02.2010 relied upon by the Department

clarify that sponsorship is an alternate form of advertisement only when associated with an event and reciprocity.

12.4 We find that Sponsorship service under Section 65(99a) is predicated upon the existence of an event and reciprocity, whereby the sponsor derives identifiable commercial or promotional benefit.

12.5 We also note that in paragraphs 15.06 to 15.15 of the Order-in-Original in the case of CUB, and paragraphs 15.06 to 15.11 of the Order-in-Original in the case of KVB, the adjudicating authority has recorded detailed findings with regard to the use of logo, brand name, and other promotional elements in connection with the sponsorship of various events (event wise). The findings are based on examination of the nature of activities and the attendant promotional benefits accruing to the appellants.

12.6 We find that pure contributions or donations made towards Corporate Social Responsibility (CSR), without any reciprocal promotional or branding benefit, do not constitute sponsorship service and is not exigible to service tax under the Finance Act, 1994. However, where the factual matrix demonstrates that the contribution is linked with visibility of the sponsor's logo, brand name, or other

promotional exposure in an event, such activity falls within the ambit of "Sponsorship Service" as defined under Section 65(99a) of the Finance Act, 1994.

12.7 In the present cases, despite the detailed findings recorded in the impugned orders, the appellants have failed to place on record any documentary evidence such as invoices, agreements, event-wise details, or other records to establish that the impugned payments were in the nature of pure CSR donations without any element of sponsorship or promotional benefit.

12.8 We also find that the appellants have contended that the impugned orders travel beyond the scope of the Show Cause Notices by allegedly introducing an "advertisement theory", and therefore the findings recorded by the adjudicating authority are liable to be set aside on this ground alone. We find no merit in this contention for the following reasons.

12.9 At the outset, we note that the Show Cause Notices proposed demand under the category of "Sponsorship Service" as defined under Section 65(99a) read with Section 65(105)(zzzn) of the Finance Act, 1994, on the ground that the appellants had sponsored various events and

activities and, in consideration thereof, had received brand visibility, logo display and promotional benefits.

12.10 The essence of sponsorship service under the statute is not confined merely to formal advertising contracts but extends to any arrangement where consideration flows for promotion of the sponsor's brand, name or logo. Therefore, references made by the adjudicating authority to advertisement or promotional benefits are only explanatory and incidental to establish the nature of sponsorship and do not amount to introduction of a new case beyond the SCN.

12.11 We further find that the impugned orders specifically record that the Board Resolutions of the appellant banks mandate that the bank's logo shall be displayed in sponsorship events and on sponsored materials/gifts. Such internal policy documents clearly demonstrate that sponsorship was undertaken with a definite commercial and promotional objective, namely enhancement of brand visibility.

12.12 In several instances, the appellants have merely asserted that the amounts paid were in the nature of donations or CSR contributions, without furnishing any documentary evidence explaining: the nature of the event,

the nexus between the event and the appellant bank, the absence of brand visibility or logo display, and why such payments should be treated as donations. In the absence of such evidence, the mere nomenclature of "donation" cannot alter the true character of the transaction.

Accordingly, we hold that: the impugned orders do not travel beyond the scope of the SCN, and the findings of the adjudicating authority are not vitiated on this ground.

12.13 In the absence of such documentary substantiation, we find no reason to interfere with the factual findings of the adjudicating authority. Mere assertions that the payments were towards CSR, without supporting evidence, cannot be accepted, particularly when the records indicate use of logo, brand name, or other promotional features.

12.14 Accordingly, we hold that the demand confirmed under the impugned orders, to the extent it pertains to sponsorship involving promotional benefits, is legal and proper, and the same is upheld.

13.1 On merits, we find that Question Nos. 1 and 2, framed by us with respect to penal interest and liquidated damages, are answered in favour of the appellants.

Consequently, the demands raised on these issues are unsustainable and are set aside.

13.2 Question No. 3, relating to Sponsorship Services, is answered in favour of the respondent/Department and against the appellants, and the demand on this count is upheld to the extent discussed hereinabove.

13.3 In view of our findings on merits in respect of Question Nos. 1 and 2, the issues relating to invocation of the extended period of limitation and imposition of penalties are rendered academic and are therefore not examined insofar as these two issues are concerned.

13.4 However, in respect of Question No. 3 relating to Sponsorship Services alone, we proceed to examine the invocation of the extended period of limitation and the imposition of penalties and record our findings accordingly.

14.1 On the question of interest, we find that interest under Section 75 of the Finance Act, 1994 is compensatory in nature. The liability to pay interest arises automatically upon delayed payment of service tax and does not depend upon the presence or absence of *mens rea*.

14.2 Once the demand relating to Sponsorship Services is upheld, interest becomes payable as a matter of law. The contention of the appellants that interest should not be levied due to interpretational issues is devoid of merit.

14.3 Accordingly, we uphold the demand of appropriate interest on the confirmed service tax liability relating to sponsorship services.

INVOCATION OF EXTENDED PERIOD OF LIMITATION: -

15.1 The appellants submitted that the issue relates to interpretation of sponsorship provisions and CSR activities. They argue that all transactions were recorded in books of accounts, audited, and there was no suppression or wilful misstatement. Hence, invocation of extended period is not justified.

15.2 The Department contends that the appellants failed to disclose the sponsorship receipts and corresponding tax liability in their ST-3 returns. Mere reflection in balance sheets does not amount to disclosure to the Department. The appellants neither sought clarification nor paid tax under protest, justifying invocation of the extended period.

15.3 We find that the appellants did not declare the impugned sponsorship transactions in their ST-3 returns nor

did they disclose the nature of such transactions to the Department at any stage prior to Audit/investigation. The service tax liability under reverse charge on sponsorship services was also not discharged. Mere accounting of the amounts in the books of accounts or disclosure in balance sheets cannot be construed as disclosure to the Department for the purposes of limitation.

15.4 Further, in *Nizam Sugar Factory v. CCE - 2006 (197) ELT 465 (SC)*, the Hon'ble Supreme Court clarified that disclosure of information in balance sheets, books of accounts or records maintained by the assessee does not amount to disclosure to the Department unless the same is specifically brought to the notice of the assessing authority. The Court held that the Department cannot be expected to infer tax liability by conducting roving inquiries into financial statements, and that non-declaration in statutory returns constitutes suppression of facts.

In the present case, the appellants admittedly did not declare the sponsorship activities or the related consideration in their statutory service tax returns. No clarification was sought from the Department, nor was tax paid under protest. Therefore, the ratio laid down in *Nizam Sugar Factory* squarely applies.

15.5 The Hon'ble Supreme Court in *Uniflex Cables Ltd. v. CCE - 2011 (273) ELT 321 (SC)* further held that when an assessee fails to disclose full and correct particulars in the statutory returns, extended period is invocable notwithstanding the fact that the information may be available in internal records or audited accounts. The Court emphasized that the obligation to disclose rests squarely on the assessee, and failure thereof attracts the proviso to the limitation section.

15.6 Applying the above settled principles to the facts of the present case, we find that the appellants' omission to disclose sponsorship services in ST-3 returns, coupled with non-payment of tax under reverse charge, constitutes suppression of material facts with intent to evade payment of service tax. The plea that the issue involves interpretation or that amounts were reflected in books of accounts does not absolve the appellants from their statutory obligation of disclosure.

15.7 Accordingly, the conditions stipulated under the proviso to Section 73(1) of the Finance Act, 1994 stand satisfied in respect of the demand relating to sponsorship services.

15.8 Accordingly, we hold that invocation of the extended period of limitation for sponsorship services is legal and proper.

Whether the demands of interest under Section 75 and penalties under Sections 77 and 78 of the Finance Act, 1994 are sustainable?

16.1 The appellants submit that penalties are not imposable as the issue relates to interpretation of the scope of "Sponsorship Services" under Section 65(99a) of the Finance Act, 1994. They contend that there was no intention to evade payment of service tax and that all transactions were duly recorded in their books of accounts. It is further argued that the appellants are scheduled banks functioning under a regulated framework and therefore penalties ought to be set aside.

16.2 The Department submits that once the extended period of limitation is held to be rightly invoked on account of suppression of material facts, penalty under Section 78 necessarily follows. It is contended that the appellants neither disclosed the sponsorship transactions in their statutory returns nor discharged service tax liability under reverse charge. Failure to comply with statutory requirements attracts penalties under Sections 77 and 78 as well.

16.3 We have already held, while examining limitation, *supra* that the appellants failed to disclose the sponsorship services in their statutory ST-3 returns and did not discharge service tax liability under reverse charge. Such non-disclosure amounts to suppression of material facts with intent to evade payment of service tax. The invocation of the extended period under the proviso to Section 73(1) of the Finance Act, 1994 has therefore been upheld.

16.4 It is a settled position of law that once suppression with intent to evade tax is established and the extended period is rightly invoked, penalty under Section 78 follows as a natural consequence. The penalty under Section 78 is attracted not merely by non-payment of tax, but by the presence of the statutory ingredients contemplated therein.

16.5 The Hon'ble Supreme Court in *Union of India v. Rajasthan Spinning & Weaving Mills – 2009 (238) ELT 3 (SC)* has held that penalty under Section 11AC of the Central Excise Act (*pari materia* to Section 78 of the Finance Act, 1994) is imposable where the conditions of suppression, wilful misstatement or intent to evade duty are satisfied. The same principle squarely applies to service tax matters.

16.6 Further, in *CCE v. Dharmendra Textile Processors – 2008 (231) ELT 3 (SC)*, the Hon'ble Supreme Court held that penalty provisions are civil liabilities and *mens rea* is not an essential ingredient once the conditions specified in the statute are fulfilled.

16.7 The appellants' plea that the issue involves interpretation of law cannot be accepted in the facts of the present case. The definition of "Sponsorship Services" and the liability under reverse charge were clearly prescribed during the relevant period. The appellants did not seek any clarification from the Department, nor did they disclose the activity in the statutory returns. Mere recording of transactions in books of accounts cannot be equated with statutory disclosure.

16.8 We also find that reliance placed by the appellants on decisions granting relief on penalty on the ground of interpretational dispute is misplaced. In the present case, the findings recorded in the Orders-in-Original establish that the sponsorship involved branding, logo display and promotional benefits, and yet the appellants chose not to discharge tax or declare the activity. Hence, such decisions are distinguishable on facts.

16.9 Penalty under Section 77 is also imposable for failure to comply with statutory obligations, including correct filing of returns and proper disclosure of taxable services.

16.10 In view of the above discussion, and having upheld the invocation of the extended period in respect of sponsorship services, we hold that penalties imposed under Sections 77 and 78 of the Finance Act, 1994 in relation to Sponsorship Services are legal and proper and do not call for interference.

17. In the result: -

- i. Question Nos. 1 and 2, relating to penal interest and liquidated damages, are answered in favour of the appellants, and the demands raised thereon are set aside.
- ii. Question No. 3, relating to Sponsorship Services, is answered in favour of the respondent/Department and against the appellants and the demand of service tax on Sponsorship Services, along with applicable interest, is upheld.
- iii. The invocation of the extended period of limitation and the imposition of penalties under Sections 77 and 78 of the Finance Act, 1994, insofar as they relate to Sponsorship Services alone, are upheld.

18. The appeals are thus partly allowed and partly dismissed, on the above terms.

(Order pronounced in open court on 22.01.2026)

Sd/-
(VASA SESHAGIRI RAO)
MEMBER (TECHNICAL)

Sd/-
(P. DINESHA)
MEMBER (JUDICIAL)

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