Negative Blues

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With the introduction of negative list based service tax levy from 01.07.2012, the learning and understanding process of the new regime should start from A…B…C….

A quick comparison of the Finance Act, 2012 with the proposals contained in the Finance Bill 2012 reveals two significant changes in the final draft.

The definition of "service" as per section clause (a) of sub section (44) of section 65B of the Finance Bill specifically excluded (i) a transfer of title in goods or immovable property, by way of sale, gift, or in any other manner. The present definition of the term "service" as per the Finance Act, 2012 has added another clause in the definition, which reads as "(ii) such transfer, delivery or supply of any goods which is deemed to be sale within the meaning of clause (29A) of article 366 of the Constitution".

By this, even deemed sale is also kept outside the levy of service tax. It may be recalled that in a bizarre decision, the Larger bench of the Hon'ble Tribunal has held in the case of Agrawal Colour Advance Photo System Vs CCE, Bhopal (2011-TIOL-1208-CESTAT-DEL-LB) that as per notification 12/2003 ST, the value of "deemed sale" cannot be excluded for the purpose of levy of service tax and in the absence of definition of the term "sale" in the Finance Act, 1994, only the definition of the term under Central Excise Act, 1944 should be referred to, which, according to the Tribunal, does not cover such deemed sale. By this amended definition of the term "service" the effect of the said decision has been overcome much to the relief of many.

The definition of the term "works contract" as per clause 65 B (54) of the Finance Bill and the present definition as per the Finance Act are reproduced below one by one.

> *"works contract means a contract wherein transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods and such contract is for the purpose of carrying out construction, erection, commissioning, installation, completion, fitting out, improvement, repair, renovation, alteration of any building or structure on land or for carrying out any other similar activity or a part thereof in relation to any building or structure on land".*
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> *"works contract means a contract wherein transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods and such contract is for the purpose of carrying out construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, alteration of any movable or immovable property or for carrying out any other similar activity or a part thereof in relation to such property".*

A comparison of the above would reveal that the specified activities even in respect of movable goods would also be construed as works contract now. While "improvement" is removed from the definition "maintenance" is added. So far, "works contract" under service tax was having only a limited coverage and not as broad as the term is understood in VAT legislations. By virtue of the present provisions, annual maintenance contracts, repairs and maintenance of goods (machines, equipments, etc) which also involves sale of goods during the course of providing such service would also be construed as "works contract" for the

purpose of levy of service tax. Hence, the scope of "works contract" under service tax levy would be very wide.

Further, it may be also be noted that if "works contract" services are performed by individuals, HUFs, proprietary concerns, partnership firms and association of persons to a business entity / company, 50 % of the service tax liability shall be discharged by the service recipient under reverse charge basis and 50 % of the liability shall be discharged by the service provider. Now, with the enhanced coverage of the term "works contract", the instances of service tax liability on service recipients under reverse charge would be more, necessitating a constant watch.

The above said "reverse charge" on works contract services would also be posing a major problem for the construction industry as explained below.

It is a common practice in the construction industry to form Joint Ventures (JVs) among various infrastructure companies, to gain competitive advantage in tendering. The status of such JVs would either be a partnership firm or Association of persons, while the constituents of the JVs would be Companies under the Companies Act. Once the work is awarded to a JV, the execution of the work would be sub contracted to one or more of the JV partners. The JV partners would raise the bill on JV and the JV would in turn raise the bill on the clients. Service tax paid by the JV partner would be availed as cenvat credit by the JV and used for payment of the service tax liability of JV. All is well so far.

With the coming into force of the new provisions, the JV, being a partnership firm or AOP, would be liable to pay only 50 % of its service tax liability, while the remaining 50 % has to be paid by the service recipient. Hence, there will be huge accumulation of cenvat credit in the hands of the JV. Since JVs are formed for a specific project, utilizing the credit for any other purpose is also ruled out. Though the CBEC's D.O. Letter on budget provisions says that suitable refund of mechanism for such accumulated credit would be introduced for small service providers, whether the JVs executing projects involving value of hundreds of crores would be considered as "small" for this purpose is doubtful.

Postscript : Rule 5 A has been introduced in Cenvat Credit Rule, 2004 to provide for refund. The relevant notification in this regard is yet to be issued.