

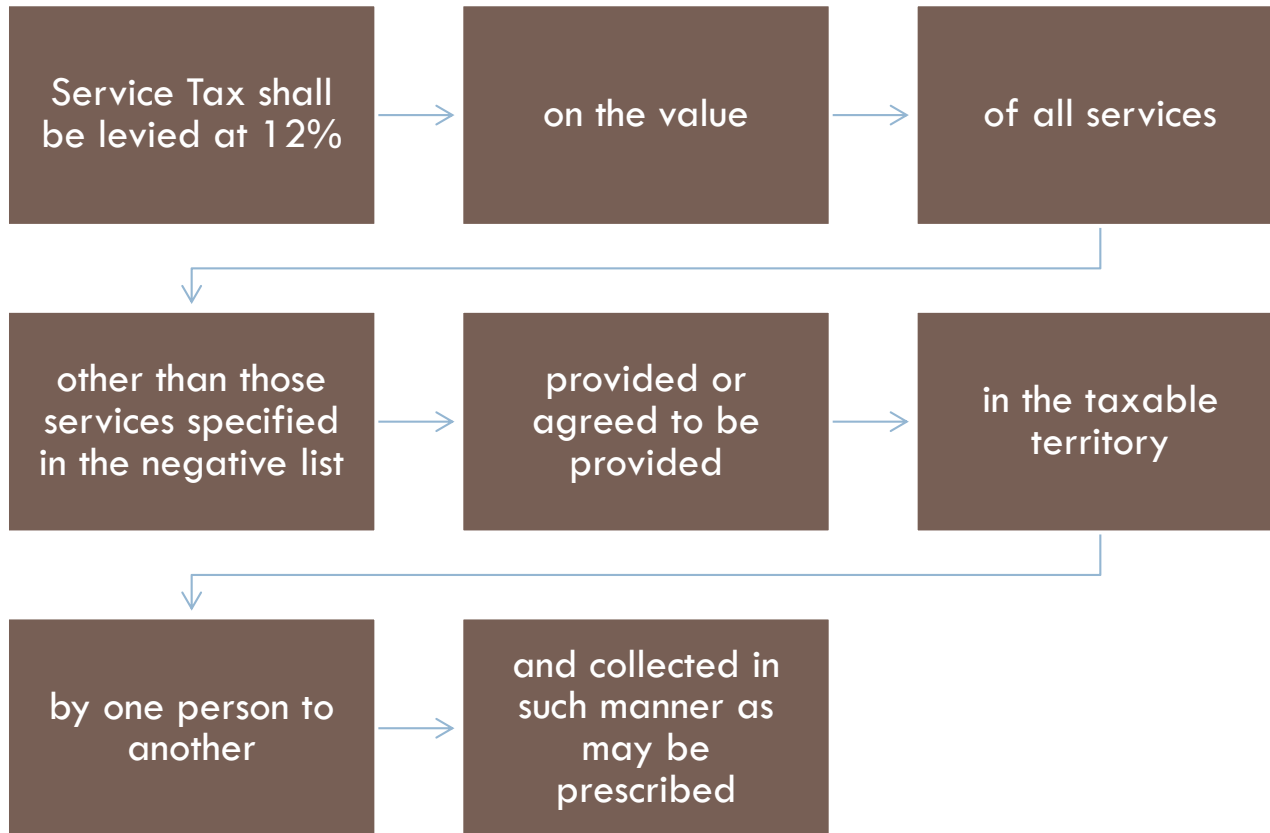
# NEGATIVE LIST BASED TAXATION OF SERVICES

# NEGATIVE LIST : FRAMEWORK

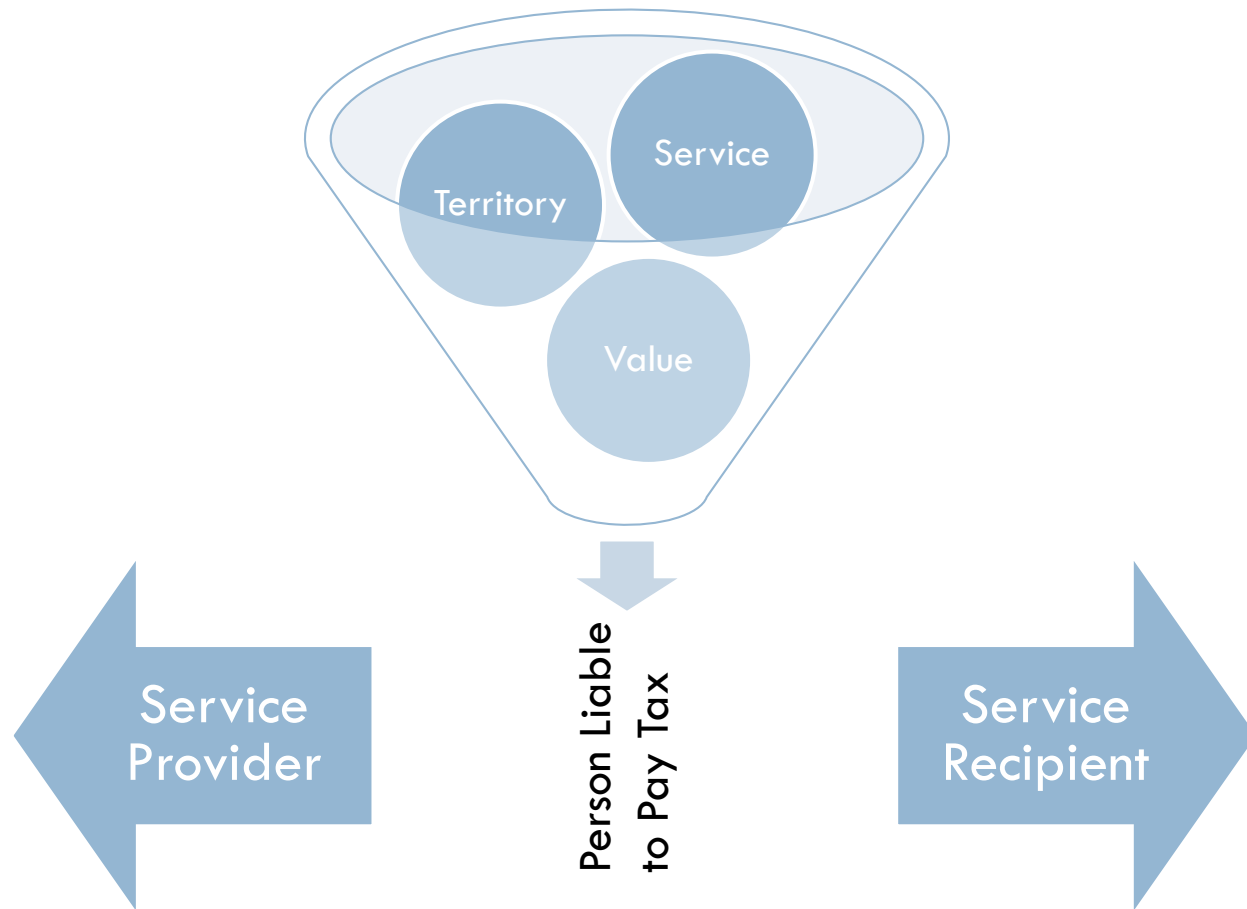


# Framework:

## Dissecting the “Charge”..



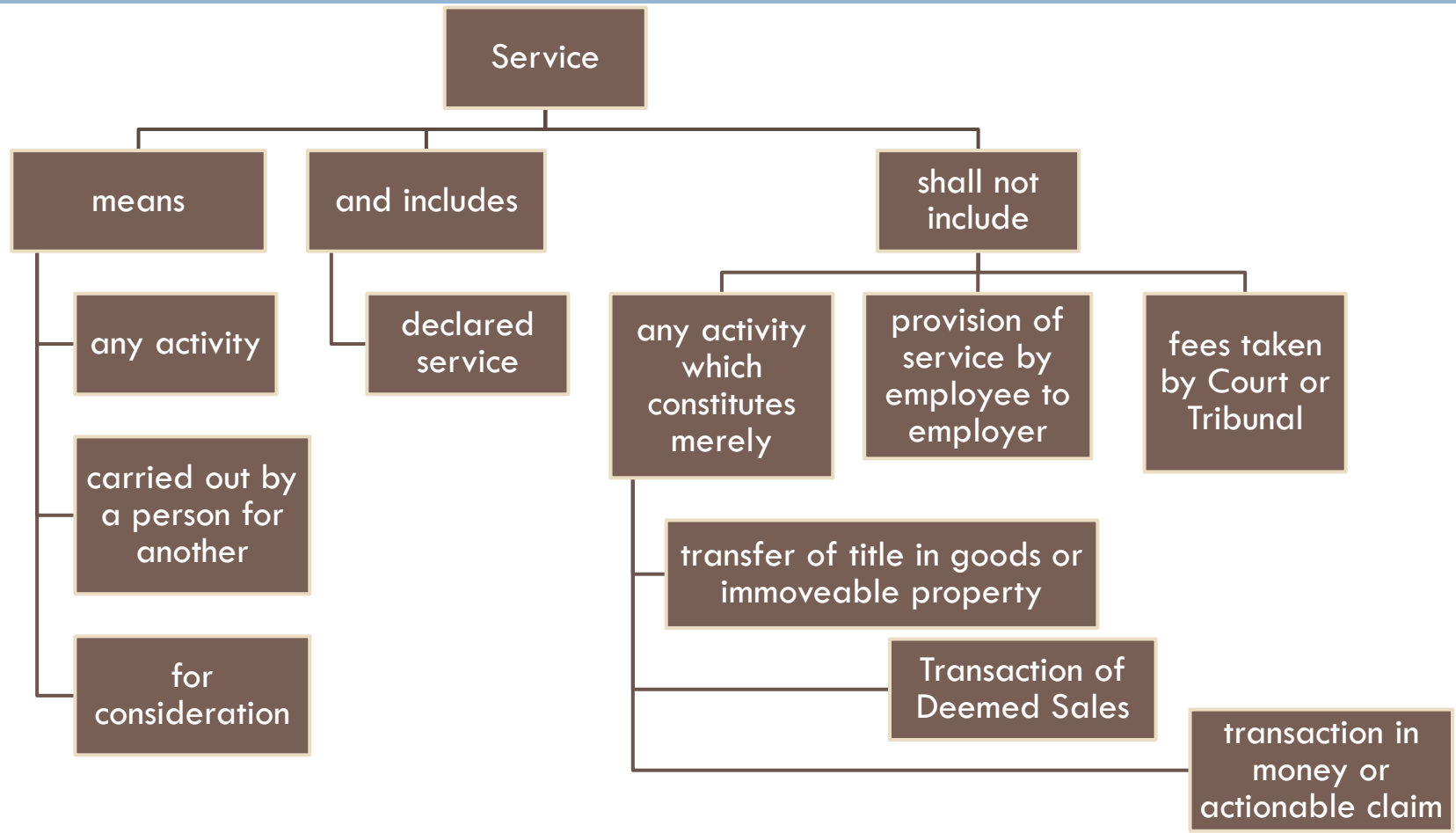
# The Elements..



# CONCEPT OF SERVICE

S B GABHAWALLA & CO

# Definition of Service



# Definition of Service : Structure

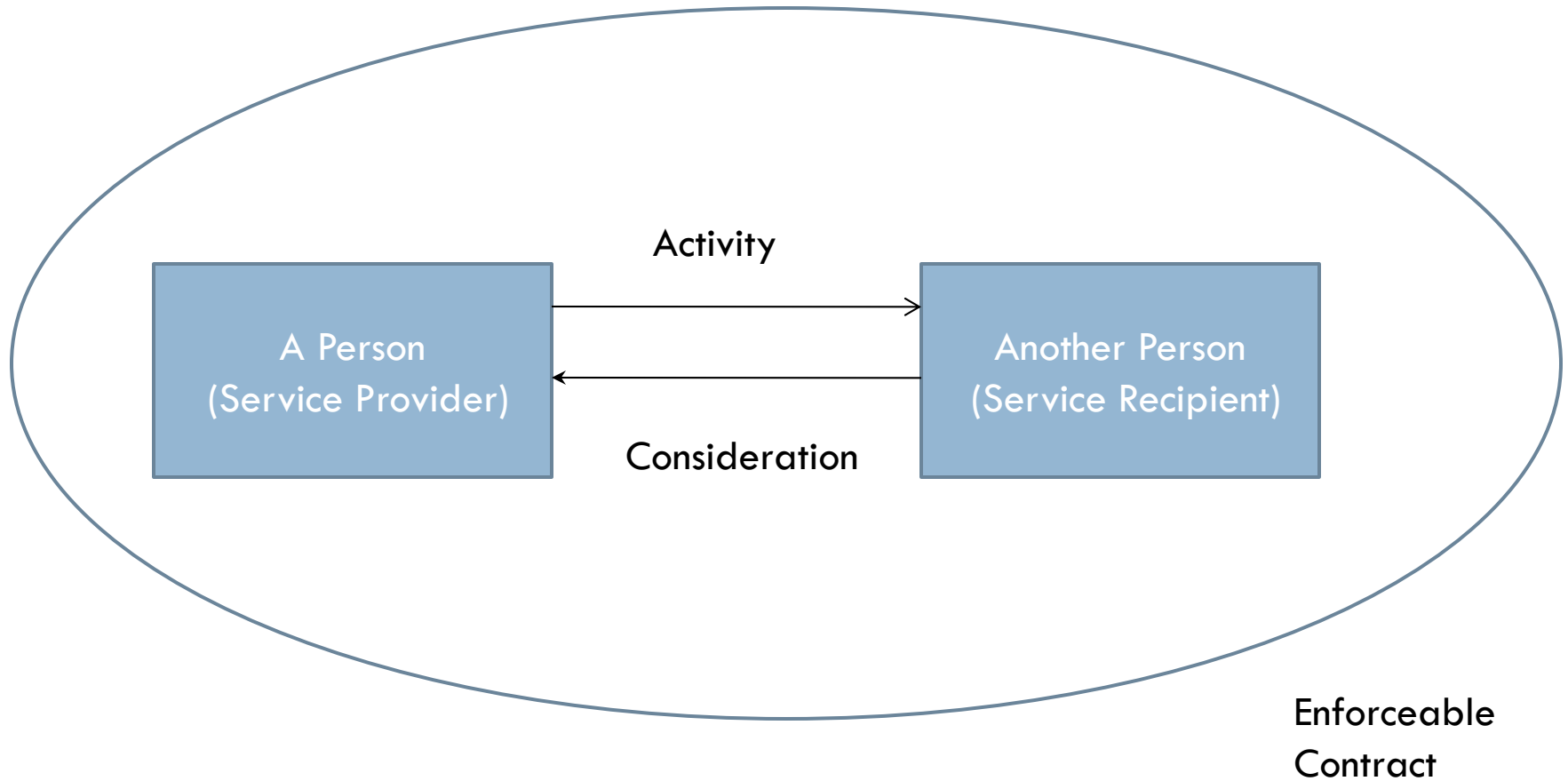
- Means – Activity for Consideration
- Includes – Declared Services
- Shall not include (IMAGE)
  - I            Immoveable Properties
  - M            Money
  - A            Actionable Claim
  - G            Goods
  - E            Employment Contracts
  
- What happens if there is a conflict between “includes” and “shall not include”?

**SERVICE : MAIN LIMB**





# Service means



# Definition of Service – “Means”

<b>Any Activity</b>	<b>Carried out by a person for another</b>	<b>For consideration</b>
Can be active or passive	Duality of Persons required	As defined under the Contract Act, 1872
Need not be economic activity	Exceptions carved out: <ul style="list-style-type: none"><li>•AOP</li><li>•Foreign Branches</li></ul>	Donations
However, not as wide as an obligation	Implication of “for”	Grants / Scholarships
		Write Backs / Excess

# Definition of Service: Nothing is “personal” ?

- Dowries received at the time of marriage
- Bribes received by a politician
- A person saving a drowning child and receiving a monetary token of appreciation from the parents of the child
- Beggar singing on road and receiving alms
- A newspaper reader completing a crossword puzzle and winning the first prize
- Amounts received by a separated son from his family as a part of family settlement.
- A person searching a missing child against whom a cash reward was announced on television
- A participant winning in reality show like Indian Idol
- Various amounts received by a co-operative society/member thereof from the developer in case of a redevelopment project.

# Duality of Persons: Deeming Fiction :

- Following are treated as distinct persons
  - ▣ An establishment of a person located in taxable territory and another establishment of such person located in non-taxable territory
  - ▣ An unincorporated association or body of persons and members thereof
  
- Will there still be a need to define an activity carried out for a consideration?

# Duality of Persons: Scope of Deeming Fiction

- Mutuality Principle Diluted
- Implications on:
  - ▣ Co-operative Societies
  - ▣ Profit Sharing Arrangements
  - ▣ Joint Ventures
  - ▣ Consortiums
- Is the deeming fiction very wide to cover cases of:
  - ▣ Friends going on contributory picnic
  - ▣ Social Groups
  - ▣ Branch Remittances

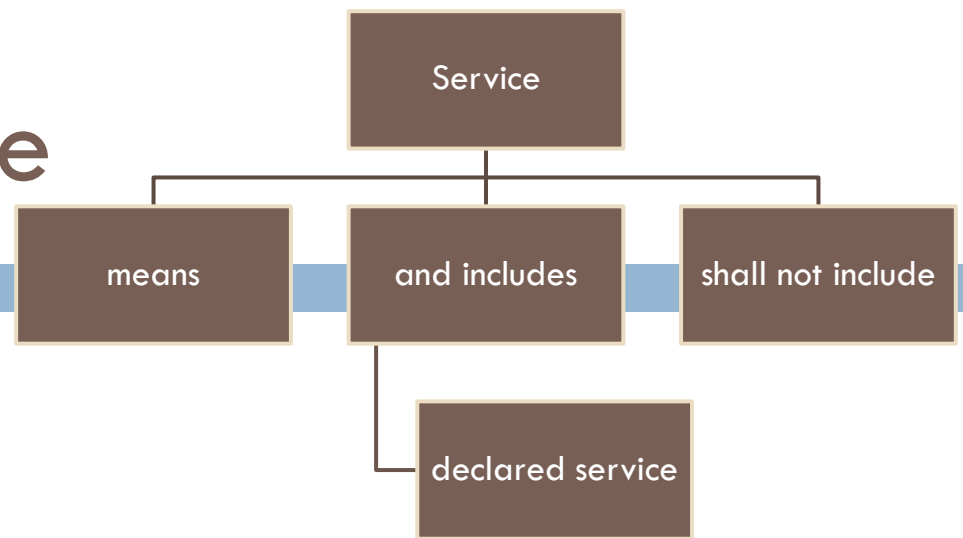
# Example of Branch Remittance:

- A Ltd. (India) has set up a branch office in Dubai. Initially, an amount of \$ 10,000 was transferred to Dubai bank account to incur expenses. Every month, further transfers are made to the branch on imprest basis
- Is there any element of service? If yes, what is the nature of the service?
- Is it a transaction only in money?

# DECLARED SERVICES

S B GABHAWALLA & CO

# Declared Service



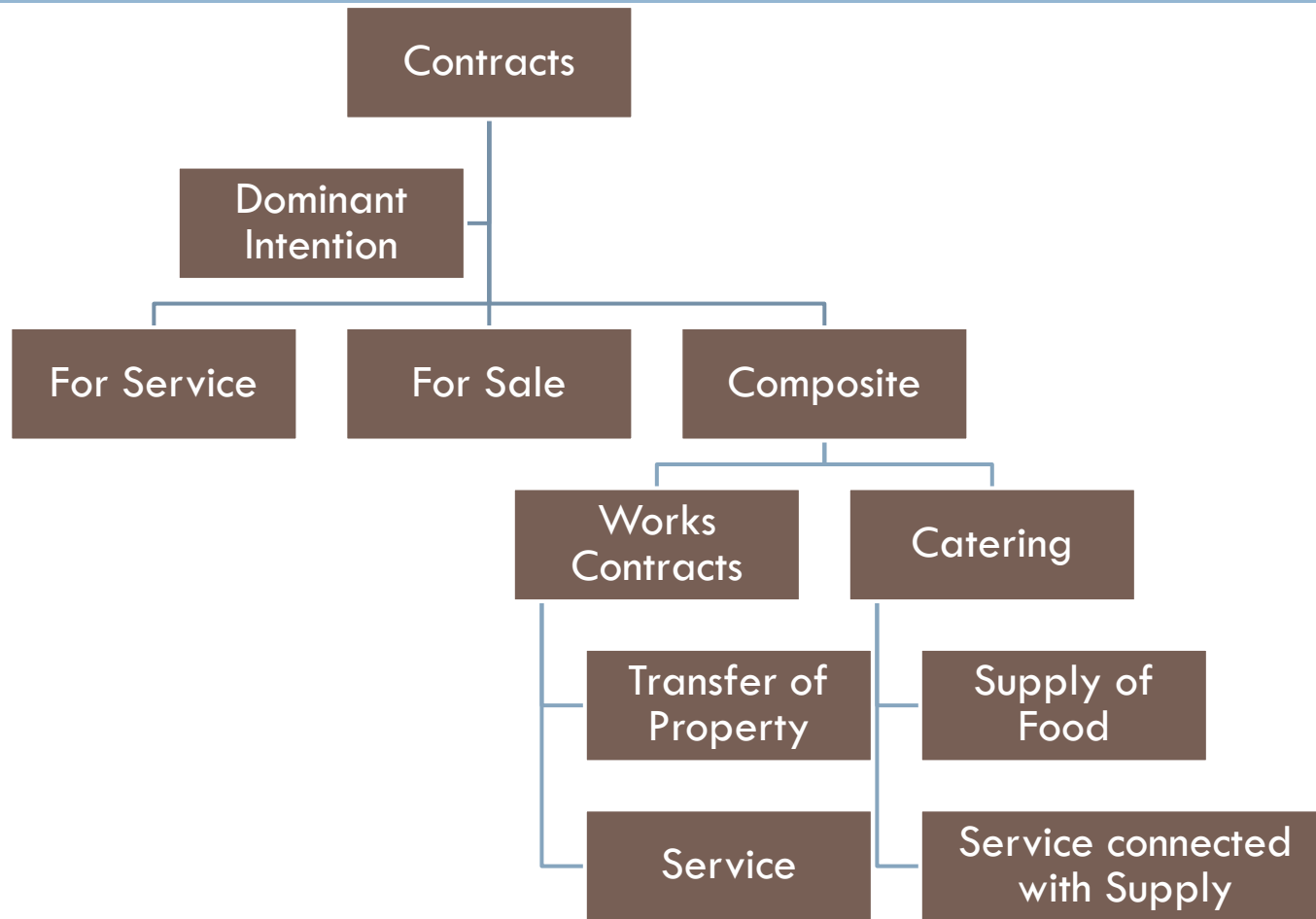
- **Immoveable Property**
  - ▣ renting of immovable property;
  - ▣ Sale of Under Construction Units
- **Leases & Licenses**
  - ▣ Temporary transfer or permitting the use or enjoyment of any intellectual property right;
  - ▣ Development, design, programming, customization, adaptation, up gradation, enhancement, implementation of information technology software;
  - ▣ transfer of goods by way of hiring, leasing, licensing or any such manner without transfer of right to use such goods;
  - ▣ activities in relation to delivery of goods on hire purchase or any system of payment by installments;
- agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act;
- service portion in execution of a works contract;
- service portion in an activity wherein goods, being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as part of the activity



# Declared Services : Issues

- Most of these represent an overlap with “deemed sale”
- However, deemed sales are excluded
- Except in case of works contracts and catering contracts, dominant intention is important to determine taxability

# Respecting the Boundaries...



# Deemed Sale vs. Declared Service

What is covered under Deemed Sale	What is covered under Declared Service
Transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract	service portion in execution of a works contract
Delivery of goods on hire-purchase or any system of payment by instalments	activities related to delivery of goods on hire- purchase or any system of payment by instalments
Transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration	transfer of goods by way of hiring, leasing or licensing or in any such manner without involving transfer of right to use goods
Supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration	service portion in an activity where such supply of food or drinks takes place

# DECLARED SERVICE 1 : RENTING



# DS1: Renting of Immovable Property...

Whether following activities are taxable?	Taxable/Non-taxable
Renting of vacant land, with or without a structure incidental to its use, relating to agriculture	Non- Taxable
Renting of residential dwelling for use as residence	Non - Taxable
Renting of any property by Reserve Bank of India	Non- Taxable
Renting of any property by a Government or a local authority to all non-business entity.	Non- Taxable
Renting of precincts of a religious place meant for general public	Non- Taxable
Renting of a hotel having declared tariff of a room below rupees one thousand per day or equivalent	Non- Taxable
Renting of a property for a temporary purpose like conduct of a marriage or any other social function.	Taxable
Renting of property to educational body	Non Taxable

# ...Renting of Immovable Property

Whether following activities are taxable?	Taxable/Non-taxable
Renting of vacant land for animal husbandry or floriculture	Non- Taxable
Use of immoveable property for vending / dispensing machines	Taxable
Allowing erection of communication tower on a building for consideration.	Taxable
Renting of land or building for entertainment or sports	Taxable
Renting of theatres by owners to film distributors	Taxable
Renting of property located outside the taxable territory but where the property is owned by a person located in the taxable territory	Non-Taxable

**DECLARED SERVICE 2:  
SALE OF UNDER CONSTRUCTION  
UNITS**



# DS2: Sale of Under Construction Units (Snapshot)

- Deeming Fiction:
  - ▣ Construction of a complex, building, civil structure or a part thereof
  - ▣ except where the entire consideration is received after issuance of completion-certificate by the competent authority
- Advance before Construction:
  - ▣ Allotment Letter
  - ▣ Agreement for Sale
  - ▣ Deposits



# DS2: Sale of Under Construction Units (Snapshot – Contd.)

- What is completion?
  - ▣ Requirement to obtain CC
    - Government or Local Authority
  - ▣ No Requirement to obtain CC
    - Architect, Engineer, Surveyor
  
- Transaction is either fully taxable or fully excluded
  
- Not Taxable if sale is after completion

# DS2: Sales of under construction units (Issues)

- What happens if there is no construction?
  - ▣ Case of investors reselling units – exempt
  - ▣ How different from builders selling first unit?
  
- Whether the exclusion clause will still prevail ?
  
  
- Past Challenge to Constitutionality of the provisions

# DS2: Sales of under construction units (Issues)

- Methods of discharging tax liability
  - ▣ Not a Works Contract so Rule 2A not applicable
  - ▣ Abatement provided through Notification so taxable component is 25%
  - ▣ Credits available under the new regime
  
- Reverse Charge Mechanism not applicable to such transactions

# DS2: Sales of under construction units (Issues)

- Need to consider tax implications of “barter” arrangements
  
- Tax Implications of
  - ▣ Development Agreement – Cash/Units/Profit Sharing
  - ▣ Redevelopment Project – Society/Members/Developer
  - ▣ Joint Development Agreement – Whether AOP?

# DS2: Sales of under construction units (Summary) ...

Whether following activities are taxable?	Taxable/Non-taxable
<p>Sale of Under Construction Units –</p> <ul style="list-style-type: none"><li>• Residential &gt; 12 Units</li><li>• Residential &lt; 12 Units</li><li>• Commercial Units</li><li>• Non Commercial Units</li></ul>	Taxable
Low- cost houses up to a carpet area of 60 square metres	Exempted
single residential unit otherwise than as a part of a residential complex;	Exempted

# **DECLARED SERVICE 3: IPR SERVICE**



## DS3: Temporary transfer or permitting the use or enjoyment of any intellectual property right

Whether following activities are taxable?	Taxable/Non-taxable
Temporary transfer of a patent registered outside India to place in India	Taxable
Temporary transfer of a patent registered in India to a place outside India.	Non-Taxable, since outside Taxable Territory
Transaction in unregistered IPRs	Taxable

- How to resolve overlap with VAT?
- What is the point of taxation?

**DECLARED SERVICE 4:  
INFORMATION TECHNOLOGY  
SOFTWARE SERVICE**





# DS4: Information Technology Software

Whether following activities are taxable?	Taxable/Non-taxable
Development, design, programming, customization, adaptation, up gradation, enhancement, implementation of information technology software	Taxable
Sale of pre-packaged or canned software	Non-Taxable, as Sales of Goods
On site development of software	Taxable
Providing a license to use prepackaged software	Not Taxable
Electronic Downloads	Taxable
Customised Software on CD	Taxable

# DS4: Information Technology Software (Various Models)

- Service
- Sale
- Periodic License
- Support
- Annual Maintenance Contract

# **DECLARED SERVICE 5: HIRE PURCHASE**



# DS5: Hire purchase

Whether following activities are taxable?	Taxable/Non-taxable
Delivery of goods on hire purchase of any system of payment by installments taxable	Non-taxable
Services connected with Hire Purchase charged as interest, lease management fee, processing fee, documentation charges and administrative fees.	Taxable

# DECLARED SERVICE 6: LEASING



# DS6: Leasing

Whether following activities are taxable?	Taxable/Non-taxable
Transfer of goods by way of hiring, leasing, licensing or any such manner without transfer of right to use such goods	Taxable
Transfer of right to use such goods	Non- Taxable

## How to differentiate ?

- There must be goods available for delivery;
- There must be a consensus ad idem as to the identity of the goods;
- The transferee should have legal right to use the goods – consequently all legal consequences of such use including any permissions or licenses required therefore should be available to the transferee;
- For the period during which the transferee has such legal right , it has to be the exclusion to the transferor – this is the necessary concomitant of the plain language of the statute, viz., a ‘transfer of the right to use’ and not merely a license to use the goods;
- Having transferred, the owner cannot again transfer the same right to others.

# Leasing Examples...

Whether following activities are taxable?	Taxable/Non-taxable
Car Hire Simpliciter (without driver)	Not Taxable
Car Hire with driver	Taxable (RCM also applies)
Equipment Hire with operator	Taxable
Trade Mark Licenses	Taxable

# **DECLARED SERVICE 7: WORKS CONTRACTS**

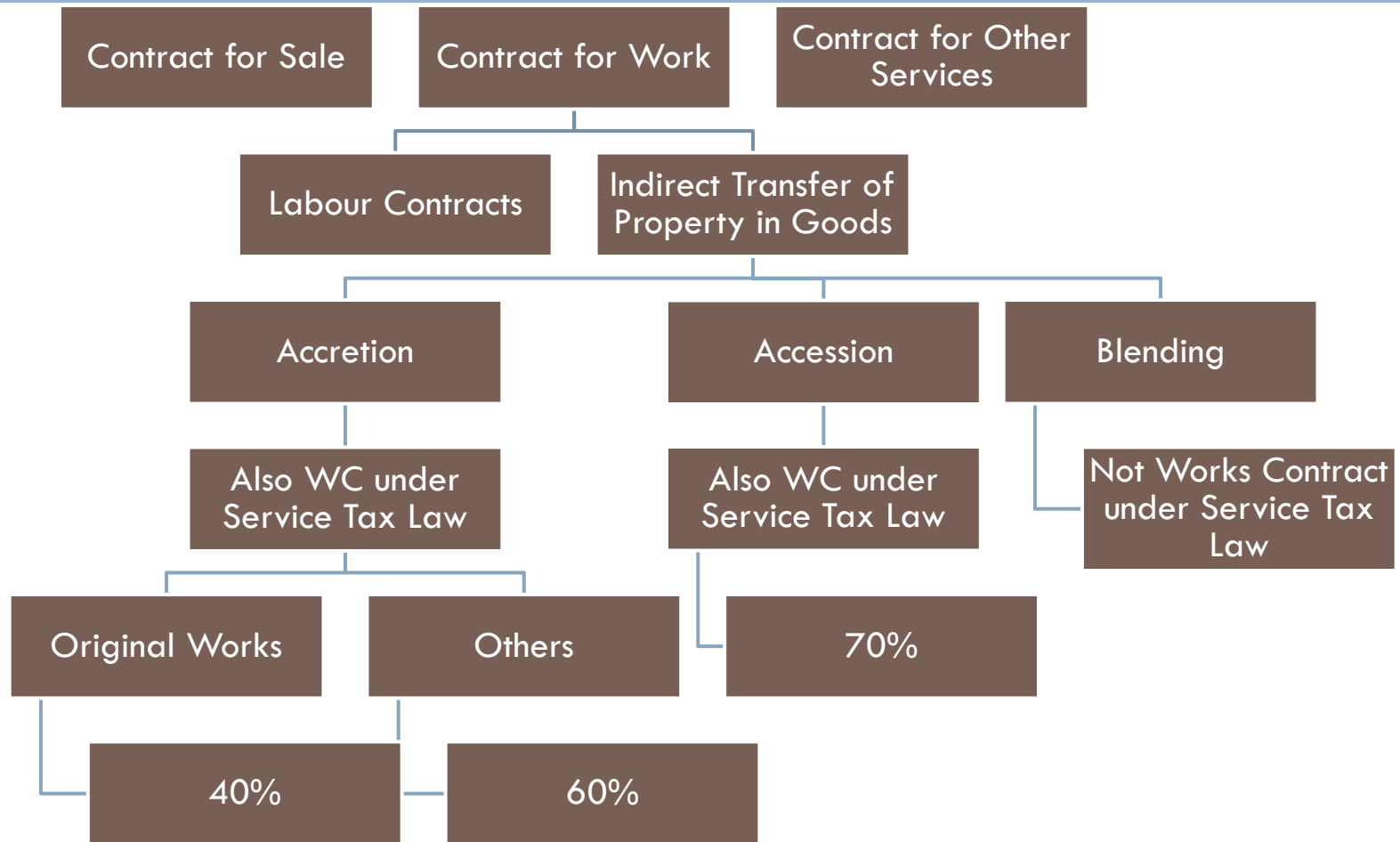




# DS7: Service portion in execution of a works contract

- Definition:
  - ▣ 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 moveable or immovable property or for carrying out any other similar activity or a part thereof in relation to such property
- Vivisection
  - ▣ Value of goods liable for VAT
  - ▣ Service Component can be taxed under Service Tax
- Goods component not a part of taxability, so credit not available

# Works Contract : General Concept



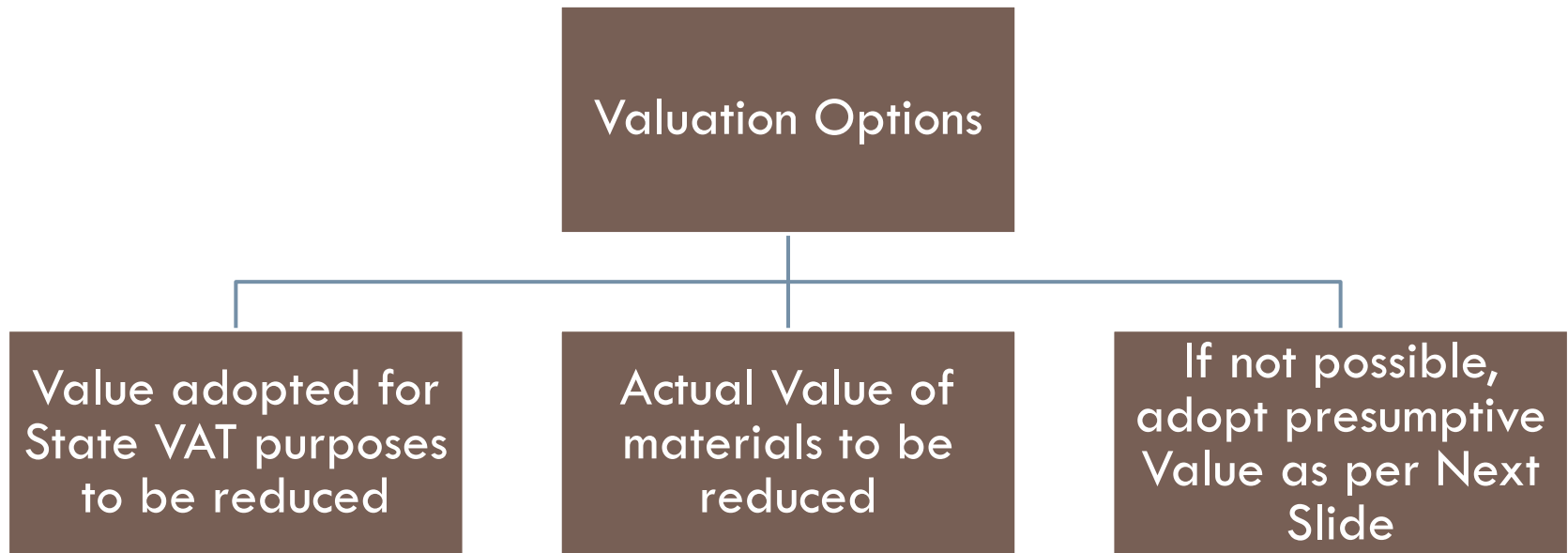
# Works Contracts : Some Examples

Example	Income Tax 94C	VAT – 29A	Service Tax – 65B(44)
<b>Treated as Works Contracts under all laws</b>			
Erection of Power Plant (on turnkey basis)	Yes	Yes	Yes
Annual Maintenance Contracts (Comprehensive)	Yes	Yes	Yes
Repairs of Motor Cars (with materials)	Yes	Yes	Yes
<b>Treated as Works Contracts under IT &amp; VAT Law but not under Service Tax Law</b>			
Printing Contracts	Yes	Yes	No
Photography Contracts	Yes	Yes	No

# Works Contracts : Some Examples

Example	Income Tax 94C	VAT – 29A	Service Tax – 65B(44)
<b>Treated as Works Contracts under IT Law but not under Service Tax or VAT Law</b>			
Construction Work undertaken on labour job basis without any transfer of material	Yes	No	No
Annual Maintenance Contracts (Non Comprehensive)	Yes	No	No
<b>Not treated as Works Contracts under any of the laws</b>			
Sale of Computer with free installation	No	No	No
Catering Contracts	No	No	No
Software Licenses	No	No	No

# Works Contract Valuation...



# ...Works Contract Valuation

<i>Nature of Works Contract</i>	<b>Presumptive Service Value</b>
i) execution of original works	40% of the <b>total amount charged</b>
ii) Works contracts connected with moveable properties	<b>70% of the total amount charged</b>
iii) works contracts, other than contracts for execution of original works, including contracts for completion and finishing services such as glazing, plastering, floor and wall tiling, installation of electrical fittings.	60% of the <b>total amount charged</b>

Total amount charged to include the value of goods or services supplied free of cost.

# Other Declared Services

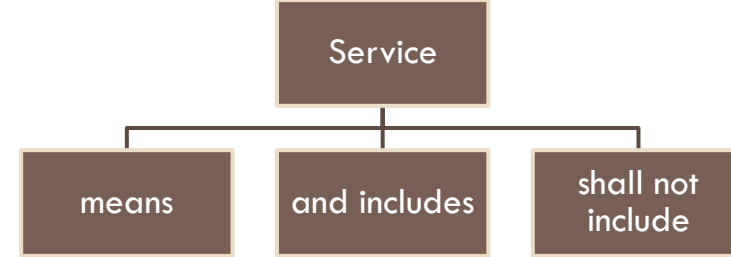
Whether following activities are taxable?	Taxable/Non-taxable
Non-compete agreements	Taxable
Agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act	Taxable
service portion in an activity wherein goods, being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as part of the activity	Taxable

# **SERVICES : EXCLUSIONS FROM DEFINITION**





# Service shall not include -



- Mere transfer of title in goods by way of sale, gift or in any other manner for a consideration (**G**)
- Mere transfer of title in immovable property by way of sale, gift or in any other manner for a consideration (**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
- Transactions only in money (**M**) or actionable claims (**A**) do not constitute service
- Provision of services by an employee to the employer is outside the ambit of services (**E**)
- Fees taken by Court or Tribunal shall not be included in the definition of service
- Explanation 1 clarifies that 'service' does not cover functions or duties performed by Members of Parliament

# Immoveable Property

- Grant of Development Rights in Land
- Sale of Superstructure
- Easement/Access Rights in Land

# Money

- Deposits / Withdrawals from Bank Accounts
- Transfer of Funds
- Sale/Exchange of Foreign Currency
- Repayment of Loans

# Actionable Claims

- Sale of Debtors
- Sale of Lottery Tickets
- Gift Vouchers
- Loyalty Coupons
- Licenses and Approvals

# Goods

- Definition
  - *"goods" means every kind of movable property other than actionable claim and money; and includes securities, growing crops, grass, and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale*
- Scope
  - Moveable Property – Tangible and Intangible
  - Securities – Shares / Units
  - Sale of Manufactured as well as Traded Goods excluded
- Issues
  - Discounts provided based on Purchases
  - Incentives provided based on Sale
  - Marketing Support
  - Discounts & Incentives provided by third parties

# Employment Contracts

- Services rendered by employee to employer are excluded
- Only if they emanate from employment contract
- No Specific Exclusion for services rendered by employer to employee

# Employee - Components

- Joining bonus
- Referral incentive
- Marketing incentive
- Overtime
- Special deputation fee
- Living Allowance

# Employee - Recoveries

- House rents
- Guest houses
- Staff canteen
- Bus transportation
- Accidental damages
- Notice period pay



# Employment Contracts : Directors

- Employee Directors excluded, non employee directors covered
- Value of Taxable Service includes
  - ▣ Sitting Fees/Commission/Remuneration
  - ▣ Reimbursement of Expenses
- Basic Threshold of Rs. 10 lakhs available
- Reverse Charge Mechanism for Foreign Directors
- Other Cases – Directors to register and comply

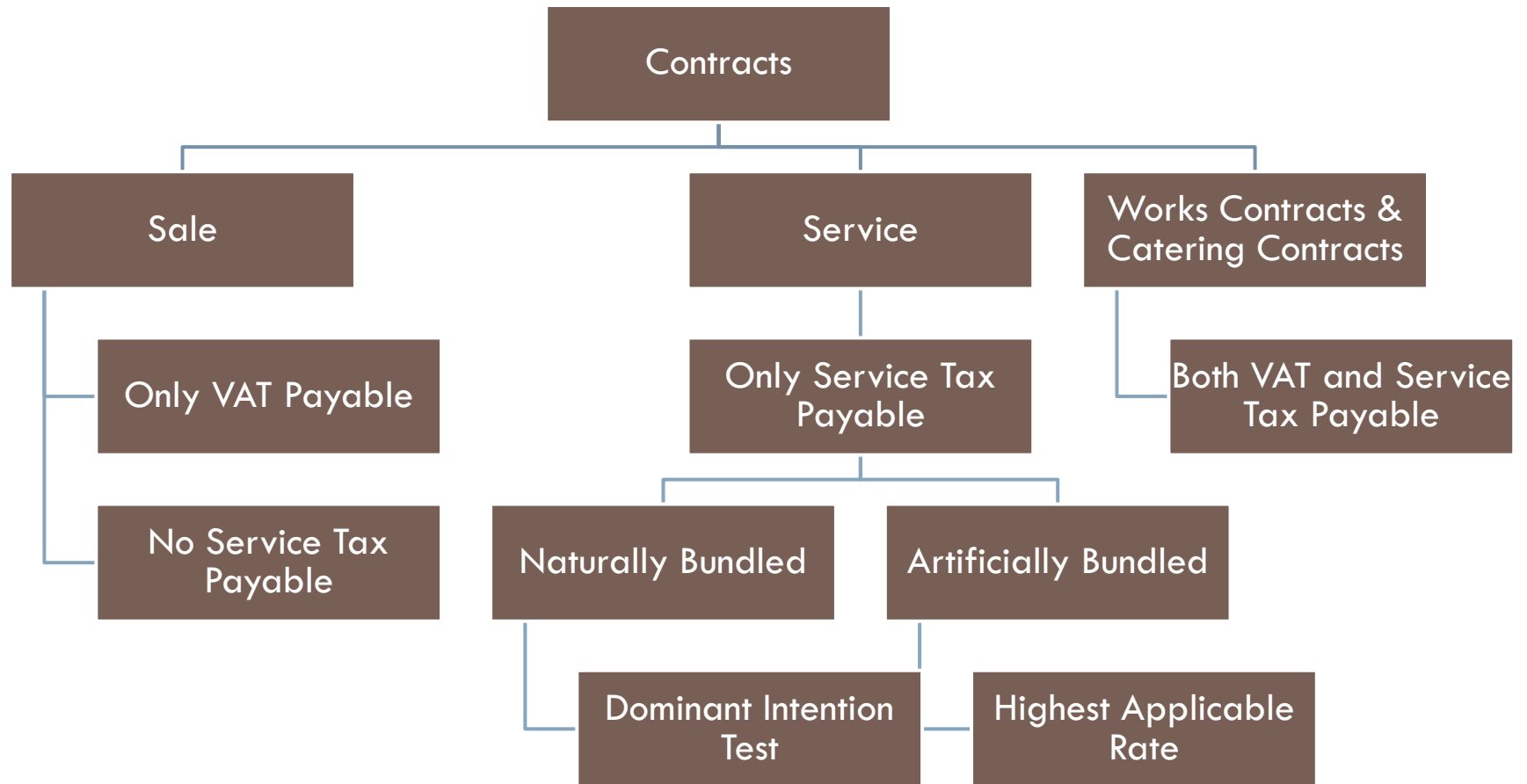
# Employment Contracts : Retainers and Consultants

- Pseudo Employees – Whether excluded?
- Value of Taxable Service includes
  - ▣ Sitting Fees/Commission/Remuneration
  - ▣ Reimbursement of Expenses
- Basic Threshold of Rs. 10 lakhs available
- Other Cases – Retainers/Consultants to register and comply

# BUNDLING OF SERVICES

S B GABHAWALLA & CO

# Gamut of Indirect Taxes: Macro Perspective



# Bundled Services

- ❑ Section 65A not applicable under Negative List
- ❑ Classification of transaction as either a service or not a service
- ❑ Transaction as a sale or service as per BSNL vs. Union of India 2006 (2) STR 161 (SC)
- ❑ Principles under section 66F for taxability of bundled services
- ❑ Nature of the output service will not determine the nature of input service
- ❑ Most specific description shall be preferred over a more general description
- ❑ 'Bundled service'
  - ▣ naturally bundled
  - ▣ not naturally bundled

# Examples on Bundled Services

- Food Supplied by Airline
- Placement Services by Educational Institution
- Loading of Goods by Goods Transport Agencies
- Sale of Print and Radio Slots as a Package
- Site Formation and Construction of Dam

# VALUATION

S B GABHAWALLA & CO

# Important Principles under Section 67

- Value of Taxable Services:
  - ▣ Gross amount charged by the service provider
  - ▣ for such service provided or to be provided by him
- No Notional Valuation Rules, however, non monetary consideration taxable
- Cum Tax Benefit Available if tax not separately charged
- Dominant Intention Test Important in contracts other than works contracts and catering contracts



# Valuation Rules

- Special Cases for Valuation:
  - Works Contracts
    - service component of composite contract (Rule 2A)
  - Money Changing
    - Service component of sale of foreign currency (Rule 2B)
  - Catering Services
    - Service Component of Supply of Food (Rule 2C)
- Reduction through Notification
- Section 67A defines the point of taxation for rate, value and exchange rate purposes

# Reimbursement of Expenses

- Any expenditure or costs incurred by the service provider
- In the course of providing taxable service
- Shall be treated as a consideration and
- Shall be included in the value for the purpose of charging service tax

# Reimbursement:

## Climb of the Everest

### □ Service Provider

- Enters into contractual arrangement
- Does not hold title to goods / services
- Does not use goods / services
- Receives actual amount
- Invoices separately the amount

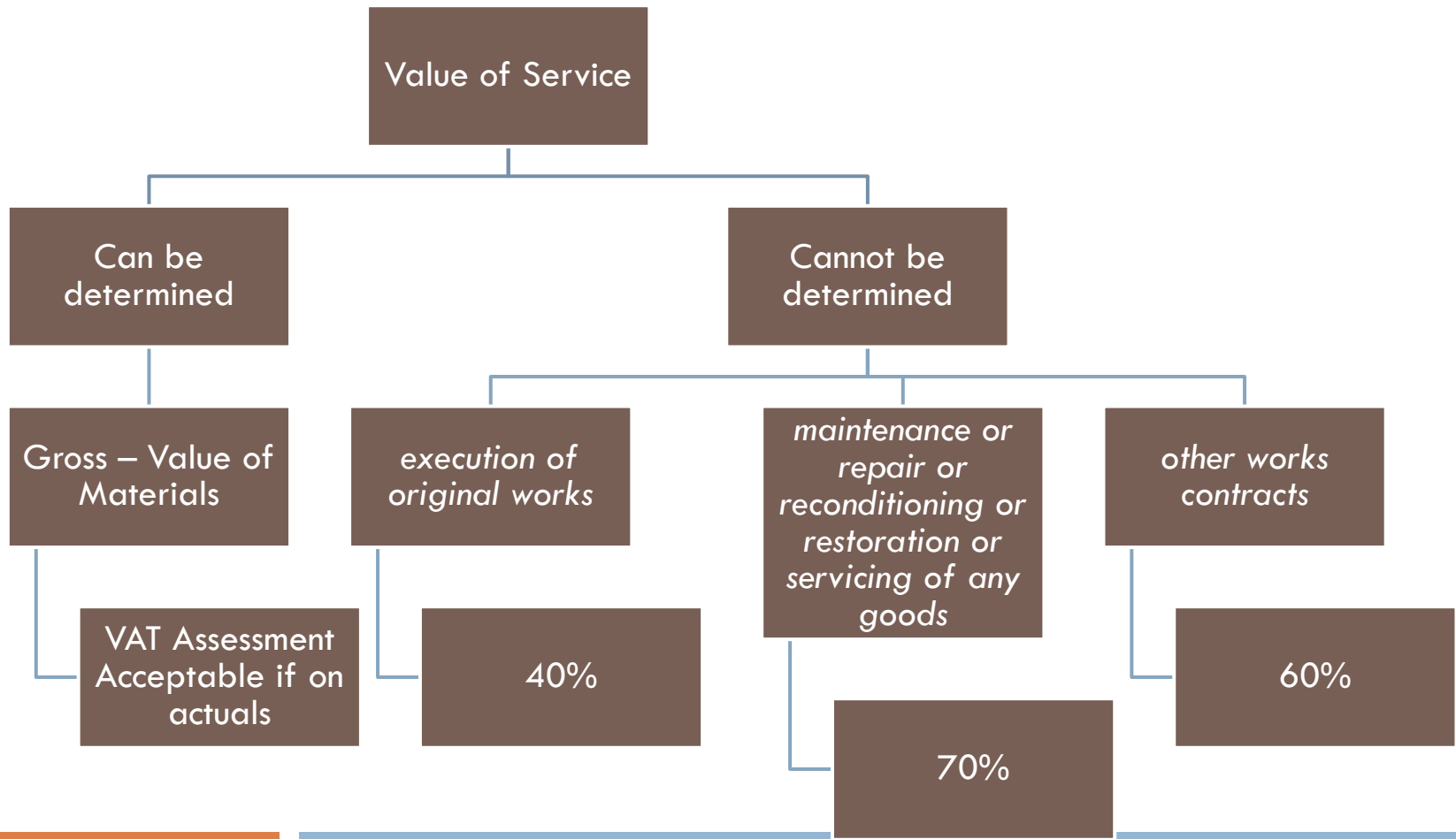
### □ Service Recipient

- Receives and uses the goods / services
- Liable to pay
- Authorises the service provider
- Knows that the services are provided by third party

### □ Service

- In Addition to the basic service

# Valuation: Works Contracts



# Valuation: Works Contracts : Issues

- If value can be determined, can presumptive method be adopted?
- If value is not adopted by the State VAT Authorities, can the actual method be adopted?
- What is the scope of inclusion of free issue materials and services?

# Restaurant & Catering

Sl. No.	Description	Percentage of the total amount
1.	Service portion in an activity wherein goods, being food or any other article of human consumption or any drink(whether or not intoxicating) is supplied in any manner as a part of the activity, at a restaurant	40
2.	Service portion in outdoor catering wherein goods, being food or any other article of human consumption or any drink(whether or not intoxicating) is supplied in any manner as a part of such outdoor catering	60

# Money Changing

Description	Rate upto 31.03.2012	Rate w.e.f. 01.04.2012
Money Changing	<b>Value = Difference between buying/selling rate and RBI Reference Rate</b>	
<b>Alternate Tax Amounts</b>		
- Upto Rs. 100000	0.1% (Min of Rs. 25)	0.12% (Min of Rs. 30)
- Between Rs. 100000 and Rs. 1000000	Rs. 100 + 0.05% of excess over 100000	Rs. 120 + 0.06% of excess over 100000
- Above Rs. 1000000	Rs. 550 + 0.01% of excess over 1000000 (Max of Rs. 5000)	Rs. 660 + 0.12% of excess over 1000000 (Max of Rs. 6000)

# Abatements through Notification

Description of taxable service	New Taxable Portion	Eligibility of CENVAT Credit on		
		Inputs	Capital Goods	Input services
Financial leasing services including equipment leasing and hire purchase	10	Yes	Yes	Yes
Transport of goods by rail	30	Yes	Yes	Yes
Transport of passengers, with or without accompanied belongings by rail	30	Yes	Yes	Yes
Supply of food or any other article of human consumption or any drink, in a premises, including hotel, convention center, club, pandal, shamiana or any place specially arranged for organizing a function	70	Yes	Yes	No (for Chap 1 to 22), Yes, for other Chap.
Transport of passengers by air, with or without accompanied belongings	40	Yes	No	No



# Abatements through Notification

Description of taxable service	New Taxable Portion	Eligibility of CENVAT Credit on		
		Inputs	Capital Goods	Input services
Renting of hotels, inns, guest houses, clubs, campsites or other commercial places meant for residential or lodging purposes	60	Yes	No	No
Transport of goods by road by Goods Transport Agency	25	No	No	No
Services provided in relation to chit	70	No	No	No
Renting of any motor vehicle designed to carry passengers	40	No	No	No
Transport of goods in a vessel from one port in India to another	50	No	No	No
Services provided or to be provided to any person, by a tour operator in relation to a package tour	25	No	No	No
Services provided by a builder	25	No	Yes	Yes