

MULUND CA CPE STUDY CIRLCE

Welcome the Members

Subject : Service Tax – Builders, Developers, Contractors and Sub Contractors

Date : Saturday, January, 18, 2014

Venue : Mulund College Auditorium. MCC College, Near Mulund Railway Station, S.N. Road, Mulund (West), Mumbai – 400 080.

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PREAMBLE

- Abbreviations:
 - The Act – Finance Act, 1994 (Service tax legislation)–amended till date
 - The Rule – Service Tax Rules, 1994 – amended till date
- Purpose of presentation is to enlighten participants about impact of negative list based levy on following sectors:
 - Real Estate
 - Construction
 - Works contract
- Scope of presentation is restricted to amendments by Finance Act, 2012 impacting the above referred sectors only.

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POSITION OF BUILDERS / DEVELOPERS TILL 30.06.2012

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SERVICE TAX – POSITION TILL 30.06.2012

- Sale of completed flats / units is a property transaction and hence, not liable to Service tax
- Legislation deemed sale of under construction flats / units to be Service provided by builder to prospective buyers w.e.f. 01.07.2010
- Abatement of 75% is available and effective tax rate:
 - Before 31.03.2012 – 2.575%
 - 01.04.2012 to 30.06.2012 – 3.09%
- Builder / Developer was not entitled to Cenvat credit of input, input services and capital goods
- Service tax levy on sale of under construction flats /units is highly litigative issue and matter is pending before Honorable Supreme Court

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PRESENT STATUS OF LITIGATION

- Honorable Punjab & Haryana High Court in **M/s G S Promoters Vs Union of India** [2010-TIOL-813] upheld constitutional validity of service tax levy on builders and developers
- Honorable Bombay High Court in **Maharashtra Chamber of Housing Industry's case** [2012-TIOL-78-HC-MUM-ST] also upheld the levy of Service tax on sale of under construction flats / units
- Honorable Supreme Court, on 30th March, 2012, admitted Special Leave Petition (SLP) challenging the above referred order of Bombay High Court
- Legal issues are still open whether:
 - Sale of under construction flats amount to provision of Service?
 - Levy of Service tax on sale of under-construction flats is constitutionally valid?
- The Honorable Supreme Court in it's recent judgment in case of Larsen & Toubro Ltd [2013- TIOL-46-SC-CT-LB] upheld that sale of under construction flat amount to works contract

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**POSITION OF BUILDERS / DEVELOPERS
ON OR AFTER 1ST JULY, 2012**

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RELEVANT PROVISIONS – ON OR AFTER 01.07.2012

- Service means [Section 65B(44) of the Act]:
 - Any activity
 - Carried out by a person for another person
 - For consideration
- It includes **declared service** (Section 66E of the Act)
 - construction of a complex, building, civil structure or a part thereof,
 - including a complex or building
 - intended for sale to a buyer, wholly or partly,
 - except where the entire consideration is received after issuance of completion-certificate by the competent authority
- It does not include:
 - An activity which constitutes merely, a **transfer of title in goods or immovable property**, by way of sale, gift or in any other manner

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SERVICE TAX IMPLICATIONS – ON OR AFTER 01.07.2012

- Sale of under construction flats/units is **declared as Service** u/s 66E(b) of the Act
- Service portion in Works contract is also declared as service u/s 66E(h) of the Act
- Definition of Service specifically **excludes** transfer of title in immovable property
- A strong view is prevalent that builders / developers transfer title in immovable property to buyer and hence transaction is not that of Service
- Old issue still remains, whether builder is:
 - Seller of property; or
 - Provider of service
- In view of specific exclusion of transfer of title in immovable property from 'service' definition, builder / developer are in better position to contend that sale of flat is not a service
- Presentation proceeds with the presumption that builders / developers are liable to Service tax

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SERVICE TAX IMPLICATIONS FOR BUILDERS – PRE and POST 01.07.2012		
Transaction	On or after 01.07.2012	Before 01.07.2012
Sale of flats/units where any part of sale consideration is received before issuance of completion certificate	Taxable – Declared Service	Taxable – Included in Definition
Sale of flats/units where entire sale consideration is received after issuance of completion certificate	Non-taxable	Non-taxable
Sale of single residential unit otherwise than as a part of a residential complex	Exempt – Clause 14(b) of Mega Exemption Notification	Non-taxable – Excluded from definition of Residential Complex
Sale of residential flats in building/complex having more than 1 unit but not more than 12 units	Taxable – No Specific exemption	Non-taxable – Excluded from definition of Residential Complex
Sale of residential flats in building/complex having more than 12 units	Taxable	Taxable

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SERVICE TAX IMPLICATIONS FOR BUILDERS – PRE and POST 01.07.2012		
Transaction	On or after 01.07.2012	Before 01.07.2012
Re-sale of flats/units	Non-taxable	Non-taxable
Sale of Entire Building (having more than 12 units) under construction to a company meant for use of its employees as staff quarters.	Taxable – No Specific exemption	Non-taxable – Excluded from definition of Complex
Sale of under construction units for commercial purpose (irrespective of number of units in a complex)	Taxable – Declared Service	Taxable – Included in Definition
Sale of under construction units to Government	Exempt – Clause 12(a) of Mega Exemption Notification	Non-taxable – Building for non-commercial purpose was excluded from definition

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SERVICE TAX IMPLICATIONS FOR BUILDERS – PRE and POST 01.07.2012		
Transaction	On or after 01.07.2012	Before 01.07.2012
Sale of residential unit predominantly meant for employees of Government, MP, MLA etc	Exempt – Clause 12(f) of Mega Exemption Notification	Non-taxable – Excluded from definition of Complex
Sale of unauthorized / unapproved flats	Taxable	Non-Taxable – Only approved residential complex were taxable
Sale of under construction flats/units to entity registered under Sec 12AA of Income tax Act, 1961 and to be used by general public for religious purpose	Exempt – Under Clause 13(c) of Mega Exemption Notification	Non-taxable – Building for non-commercial purpose was excluded from definition
Sale of units to charitable trusts for educational / hospital / clinic etc	Taxable – No specific exemption	Non-taxable – Same as above
<ul style="list-style-type: none"> ➤ “Single residential unit” means a self contained residential unit designed for residential use for one family ➤ “Residential complex” means any complex consisting of a building or buildings having more than one single residential unit 		
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EFFECTIVE TAX RATE FOR SALE OF UNDER CONSTRUCTION FLATS / UNITS – w.e.f. 01.07.2012					
➤ Notification No. 26/2012 dt 20.07.2012 notified changes in abatement					
Taxable Service	Position from 01.07.2012 to 28.02.2013		Position Upto 30.06.2012		Impact
	Taxable Value	Effective Tax	Taxable Value	Effective Tax	
Sale of under construction flats/units where any consideration is received before issuance of completion certificate <u>provided</u> value of land is included in consideration	25	3.09	25 25	2.575 3.09*	☹
Cenvat availability of:					
Inputs (such as cement, steel etc)	Not available		Not available		☺
Input Services (such as architect, contractor etc.)	Available		Not available		
Capital Goods (such as machinery, equipment etc.)	Available		Not available		
* From 01-04-2012 to 30-06-2012					
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EFFECTIVE TAX RATE FOR SALE OF UNDER CONSTRUCTION FLATS / UNITS – 01.03.2013 TO 07.05.2013				
➤ Notification No. 02/2013 dt. 01.03.2013 notified changes in abatement				
Particulars	Abatement	Taxable Position	Effective Rate	Conditions / Remark
i. Residential unit having carpet area upto 2000 sq. ft. or less irrespective of value of sale consideration	75%	25%	3.09%	• No Cenvat for input • Sale value to include the land value • Cenvat available for input services • Cenvat available for capital goods
ii. Residential unit having consideration of less than Rs.1 Crore irrespective of area of the flat	75%	25%	3.09%	
For other than above:				
i. Residential unit having carpet area more than 2000 sq. ft. and consideration is Rs. 1 Crore or more	70%	30%	3.708%	• Cenvat available for input services • Cenvat available for capital goods
ii. Commercial unit irrespective of area or value	70%	30%	3.708%	
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EFFECTIVE TAX RATE FOR SALE OF UNDER CONSTRUCTION FLATS / UNITS – w.e.f. 08.05.2013				
➤ Notification No 09/2013 dt. 08.05.2013 notified changes in abatement				
Particulars	Abatement	Taxable Position	Effective Rate	Conditions / Remark
Residential unit having carpet area upto 2000 sq. ft. or less and consideration is less than Rs. 1 Crore	75%	25%	3.09%	• No Cenvat for input • Sale value to include the land value • Cenvat available for input services • Cenvat available for capital goods
For other than above:				
i. Residential unit having carpet area more than 2000 sq. ft. irrespective of value of sales consideration	70%	30%	3.708%	• Cenvat available for input services • Cenvat available for capital goods
ii. Residential unit having sales consideration of Rs.1 Crore or more irrespective of area of the flat	70%	30%	3.708%	
iii. Commercial unit irrespective of area or sale value	70%	30%	3.708%	
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BUILDERS / DEVELOPERS – SOME ISSUES		
➤	Whether preferential location and floor rise charges are taxable at 12.36% or 3.09% ?	
➤	Whether sale of following are liable to Service tax:	
	Development right	FSI
		TDR
➤	Whether builder is liable to service tax in respect of flats allotted to :	
	<ul style="list-style-type: none">• Land Owner in lieu of land development rights.• Existing members of the society in redevelopment project.• Hutment occupants in case of SRA project.	
➤	Whether land owner (getting the flats in lieu of sale of development rights) is liable to service tax in respect of such flats sold during construction by him?	
➤	Builder started construction of Residential complex having 10 units in 2011. Whether progress payments due on or after 01.07.2012 liable to tax?	
➤	Whether builder will have to reverse proportionate Cenvat relatable to sale of completed flats on which no Service tax is payable?	
➤	Whether completion certificate issued by an architect , Chartered engineer or license surveyor is still a valid certificate post 01.07.2012?	
➤	Whether advance against maintenance is liable to service tax?	

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<p>POSITION OF CONTRACTORS / INFRASTRUCTURE PROJECTS ON OR AFTER 1ST JULY, 2012</p>

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SERVICE TAX IMPLICATIONS FOR GOVERNMENT JOBS– PRE and POST 01.07.2012 (Clause 12 of mega exemption notification)		
Transaction	On or after 01.07.2012	Before 01.07.2012
Services provided to Government, local authority or Governmental authority by way of construction of:		
(i) Civil structure / Original works for use other than commerce, industry or any other business or profession	Exempt	Non-taxable
(ii) Historical monuments / archeological site	Exempt	Non-taxable
(iii) Structure predominantly for educational, clinical, art or cultural establishment	Exempt	Non-taxable
(iv) Canal, dam or other irrigation works	Exempt	Non-taxable
(v) Pipeline, conduit or plant for water supply, water treatment, sewerage treatment/disposal	Exempt	Litigative issue
(vi) Residential complex predominantly for its employees, MP, MLA etc	Exempt	Non-taxable

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SERVICE TAX IMPLICATIONS FOR GOVERNMENT JOBS– PRE and POST 01.07.2012 (Clause 12 of mega exemption notification)		
Transaction	On or after 01.07.2012	Before 01.07.2012
(vii) By way of erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation or alteration of all the above	Exempt	Litigative issue
All above services to Government for commerce, industry or for any other business or profession (for example – construction of warehouse, industrial units etc. for sale)	Taxable	Taxable

➤ Retrospective exemption granted for Management, Maintenance or repair services during the period 16.06.2005 to 26.07.2009 in respect of non-commercial government buildings

➤ Service provider entitled to claim refund of such tax within 6 months from 28.05.2012 (enactment date)

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SERVICE TAX IMPLICATIONS FOR INFRASTRUCTURE PROJECTS – PRE and POST 01.07.2012 (Clause 13 of mega exemption notification)		
Transaction	On or after 01.07.2012	Before 01.07.2012
Services provided to any person by way of construction of:		
(i) Road	Exempt, if for general public use	Non-taxable even if for private use
(ii) Bridge	Exempt, if for general public use	Non-taxable even if for private use
(iii) Tunnel	Exempt, if for general public use	Non-taxable even if for private use
(iv) Road transport terminal	Exempt, if for general public use	Non-taxable even if for private use
(v) Civil structure or original works under JNNURM or RAY	Exempt	Non-taxable

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SERVICE TAX IMPLICATIONS FOR INFRASTRUCTURE PROJECTS – PRE and POST 01.07.2012 (Clause 13 of mega exemption notification)		
Transaction	On or after 01.07.2012	Before 01.07.2012
(vi) Building owned by a entity registered under Sec 12AA of Income tax Act, 1961 and to be used by general public for religious purpose	Exempt, if for general public use	Non-taxable
(vii) Construction/Erection of pollution control or effluent treatment plant (other than as a part of factory)	Exempt	Taxable
(viii) Construction/Erection of structure meant for funeral, burial or cremation	Exempt	Non-taxable

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SERVICE TAX IMPLICATIONS FOR INFRASTRUCTURE PROJECTS – PRE and POST 01.07.2012 (Clause 13 of mega exemption notification)		
Transaction	On or after 01.07.2012	Before 01.07.2012
Repair, renovation, commissioning, installation, completion, fitting out, maintenance, or alteration of all the above	Exempt	Litigative issue
Construction of hospital, educational institutions such as schools, colleges, etc by charitable trusts or NGO's	Taxable	Non-taxable
<ul style="list-style-type: none"> ➤ Retrospective exemption granted for Management, Maintenance or repair services during the period 16.06.2005 to 26.07.2009 in respect of road ➤ Service provider entitled to claim refund of such tax within 6 months from 28.05.2012 (enactment date) 		

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SERVICE TAX IMPLICATIONS FOR INFRASTRUCTURE PROJECTS – PRE and POST 01.07.2012 (Clause 14 of mega exemption notification)		
Transaction	On or after 01.07.2012	Before 01.07.2012
Services provided to any person by way of construction, erection, commissioning or installation of:		Non-taxable in case of works contract. Labour contract for Erection, commissioning etc was taxable.
(i) Airport	Exempt	
(ii) Port	Exempt	
(iii) Railway, including monorail or metro	Exempt	
(iv) Single residential unit otherwise than as a part of residential complex	Exempt	Non-taxable
(v) Low cost houses in approved housing projects upto a carpet area of 60 square meters per house	Exempt	No specific exemption
(vi) post-harvest storage infrastructure for agricultural produce including a cold storage	Exempt	Exempt by Notification

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SERVICE TAX IMPLICATIONS FOR INFRASTRUCTURE PROJECTS – PRE and POST 01.07.2012 (Clause 14 of mega exemption notification)		
Transaction	On or after 01.07.2012	Before 01.07.2012
(vii) Mechanized food grain handling system, machinery or equipment for units processing agricultural produce as food stuff excluding alcoholic beverages	Exempt	Exempt by Notification
Repair, maintenance, alteration, renovation etc of all above items	Taxable	Litigative issue

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TAXABILITY OF SUB-CONTRACTORS
<ul style="list-style-type: none"> ➤ Sub-contractors are independent assesseees liable to Service tax. Merely main contractor or builder pays Service tax, sub-contractor is not automatically exempted ➤ Clause 29(h) of Mega exemption Notification No 25/2012-ST dated 20.06.2012 provides for exemption to sub-contractor providing: <ul style="list-style-type: none"> • works contract services • to main contractor providing exempt Works Contract services ➤ Sub-contractor providing labour services (other than works contract services) is not entitled to above referred exemption ➤ Pre-amendment, sub-contractor was entitled to such exemption in respect of works contract services and labour contract services also

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Contractors/ sub contractors- issues

- Contactor commenced construction of charitable hospital in 2011. Whether progress payments due on or after 01.07.2012 liable to tax?
- Exemption notification no.13 allows an exemption in respect of civil structures which are meant for use of general public. In absence of definition of general public, what meaning should be assigned to this term?
- Whether sub contractor is entitled to exemption for providing works contract and/or labour contract service to main contractor in respect of following :
 - Construction of civil structure in SEZ/for SEZ developers
 - Construction of civil structure in respect of government building which is exempt under clause 12 of mega exemption notification.
 - Infrastructure projects such as road, bridge, temple, airport etc which are exempt under clause 13 and 14 of mega exemption notification.

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WORKS CONTRACT SERVICE

w.e.f. 01.07.2012

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MEANING OF WORKS CONTRACT															
<p>➤ Service portion in works contract is declared as service u/s 66E(h) of the Act</p> <p>➤ Works contract service means [Section 65B (54)] :</p> <ul style="list-style-type: none"> • Contract involving transfer of goods in execution of such contract • such transfer of goods is leviable to tax as sale of goods; and • such contract is for carrying out: <table border="1" style="margin-left: 40px; border-collapse: collapse; text-align: center;"> <tr> <td style="padding: 2px 5px;">Construction</td> <td style="padding: 2px 5px;">Erection</td> <td style="padding: 2px 5px;">Commissioning</td> <td style="padding: 2px 5px;">Installation</td> </tr> <tr> <td style="padding: 2px 5px;">Completion</td> <td style="padding: 2px 5px;">Fitting out</td> <td style="padding: 2px 5px;">Repair</td> <td style="padding: 2px 5px;">Maintenance</td> </tr> <tr> <td style="padding: 2px 5px;">Alteration</td> <td style="padding: 2px 5px;">Renovation</td> <td colspan="2" style="padding: 2px 5px;">Other similar activity</td> </tr> </table> <p style="margin-left: 40px;">of / in respect of movable or immovable property</p> <p>➤ <u>Prior to 01/07/2012</u>, works contract meant works contract in respect of immovable property</p> <p>➤ Now it includes works contract in respect of goods / movable property also</p>				Construction	Erection	Commissioning	Installation	Completion	Fitting out	Repair	Maintenance	Alteration	Renovation	Other similar activity	
Construction	Erection	Commissioning	Installation												
Completion	Fitting out	Repair	Maintenance												
Alteration	Renovation	Other similar activity													
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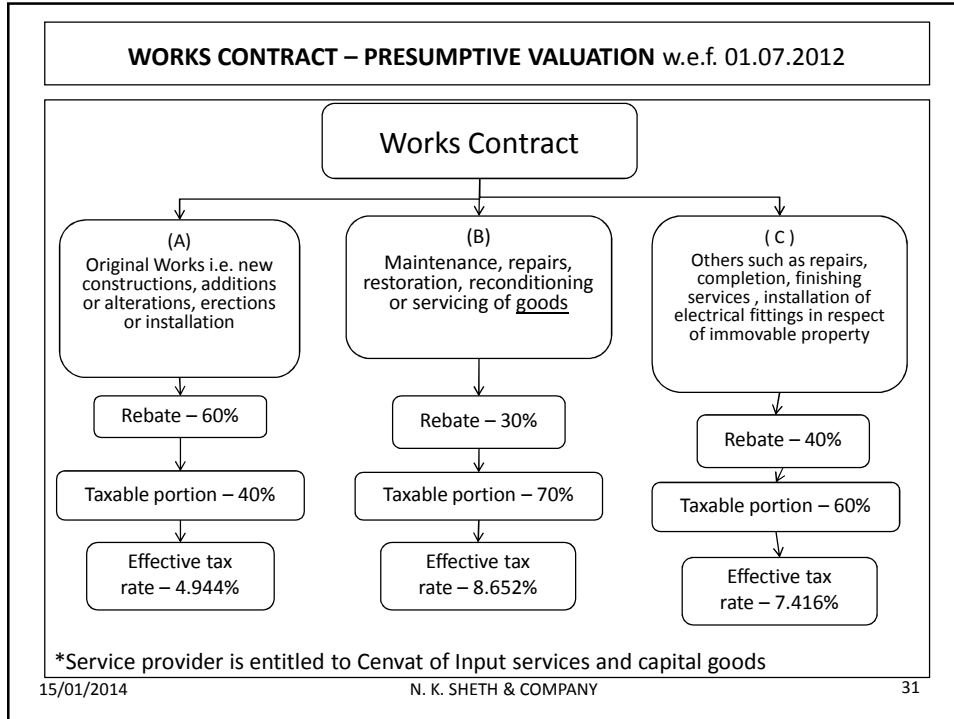
WORKS CONTRACT - Categories	
<p>➤ “Original work” means [Explanation 1 to Rule 2A (ii)]:</p> <ul style="list-style-type: none"> • all new constructions • all types of additions and alteration to abandoned / damage structures on land that are required to make them workable • Erection, commissioning or installation of plant, machinery or equipment or structures, whether pre-fabricated or otherwise <p style="margin-left: 40px;">- Category A</p> <p>➤ Works contract for maintenance, repair, reconditioning, restoration or servicing of goods is separately distinguished from “original work” and “other works”</p> <p style="margin-left: 40px;">- Category B</p> <p>➤ “Other works” means:</p> <ul style="list-style-type: none"> • Works contract other than original work (Category A) or falling in Category B • It includes maintenance, repairs , completion and finishing services such as glazing, plastering, floor and wall tiling, electrical fittings of an immovable property <p>➤ Service provider is entitled to Cenvat of input services and capital goods irrespective of valuation method / scheme adopted.</p> <p>➤ Service provider is not entitled to Cenvat of inputs.</p>	
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VALUATION OF WORKS CONTRACT SERVICE - w.e.f. 01.07.2012	
<ul style="list-style-type: none"> ➤ Pre 01.07.2012, Assessee had a choice of working out specific value of Services under Rule 2A of Valuation Rules or under Composition Scheme ➤ The composition scheme is withdrawn w.e.f. 01.07.2012 and Rule 2A has been revised ➤ Revised Rule 2A of Valuation Rules : <ul style="list-style-type: none"> • Value of service portion shall be gross amount of works contract less value of goods (material) transferred in execution of contract. <ul style="list-style-type: none"> • VAT / Sales Tax to be excluded from gross amount of works contract. • Where vat/sales tax has been paid or payable on <u>actual</u> value of goods transferred in execution of contract, such value should be taken for determining value of service portion. 	
Gross Contract Value	A
(less) VAT / Sales tax	B
(less) value of goods	C
Taxable Value	D = (A – B – C)
Tax payable would be 12.36% of D	

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VALUATION OF WORKS CONTRACT SERVICE - w.e.f. 01.07.2012									
<ul style="list-style-type: none"> • Value of service should include following specified overheads : <table border="1" style="width: 100%; margin-top: 5px; border-collapse: collapse;"> <tbody> <tr> <td style="width: 50%;">Labour / service charges paid</td> <td style="width: 50%;">Sub-contractor charges</td> </tr> <tr> <td>Planning, designing, architect fees</td> <td>Tools / machinery hire charges</td> </tr> <tr> <td>Water, electricity, fuel, consumables</td> <td>Establishment cost</td> </tr> <tr> <td>Expenses relatable to services</td> <td>Profit relatable to services</td> </tr> </tbody> </table> • Where value of service is not determined as above, value of the service would be specified percentage of contract value (presumptive Scheme) [Refer Slide No.31] 		Labour / service charges paid	Sub-contractor charges	Planning, designing, architect fees	Tools / machinery hire charges	Water, electricity, fuel, consumables	Establishment cost	Expenses relatable to services	Profit relatable to services
Labour / service charges paid	Sub-contractor charges								
Planning, designing, architect fees	Tools / machinery hire charges								
Water, electricity, fuel, consumables	Establishment cost								
Expenses relatable to services	Profit relatable to services								
<ul style="list-style-type: none"> ➤ Even for presumptive scheme, the vat or sales tax to be excluded from gross contract value. Service provider is entitled to Cenvat of input services and capital goods irrespective of valuation method / scheme adopted ➤ Service provider is not entitled to Cenvat of inputs 									

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WORKS CONTRACT – Inclusion of Material / Service Value

➤ Rule 2A (ii) (D) - “total amount” for presumptive taxation :

Gross Amount Charged for Works Contract	A
Add : Fair Market Value of All Goods Supplied in or in relation to execution of works contract (Under same contract or separate contract)	B
Add : Fair Market Value of All Services Supplied in or in relation to execution of works contract (Under same contract or separate contract)	C
Less: Amount Charged for above goods / services	D
Less: VAT / Sales Tax levied thereon	E
Total Amount on which tax to be worked out (A+B+C-D-E)	F
Tax at presumptive rate on F	

➤ Fair Market Value of Goods and services so supplied may be determined in accordance with Normally accepted accounting principles?

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Applicability of Reverse Charge Mechanism				
➤ Reverse charge mechanism is applicable w.e.f. 01.07.2012 when :				
Nature of Service	Service provider	Service recipient	Liability of Service Provider	Liability of Service Receiver
Works Contract	Individual/HUF or Partnership Firm or AOP	Business entity registered as body corporate located in taxable territory	50%	50%
Original Work			(2.472%)	(2.472%)
Repair / AMC of goods			(4.326%)	(4.326%)
Other Work			(3.708%)	(3.708%)
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WORKS CONTRACT – SOME ISSUES		
➤ Whether all Works Contract under VAT are Works Contract under Service Tax ?		
➤ In case where contractor has paid vat on actual basis, whether he is entitled to presumptive valuation for service tax?		
➤ In case where contractor pays VAT under composition scheme (Where value of material is not declared for VAT purpose), whether contractor is obliged to follow presumptive scheme of valuation or he can follow specific valuation?		
➤ What will be the applicable rate of Service tax in respect of following finishing and completion contracts for new construction:		
Plastering	Tilling	Painting
Electrical	Plumbing	Carpentry
➤ Whether site formation and clearance contractor can charge Service tax claiming rebate for new constructions?		
➤ Controversy as to inclusion of free material supplied by client or material supplied at concessional value – Impact of decision of larger bench of delhi tribunal in case of Bhayana Builders (P) Ltd [2013-TIOL-1331]		
➤ <u>Overlapping of VAT and service tax on certain contracts</u>		
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WORKS CONTRACT – SOME ISSUES

- Whether Service tax paid under reverse charge mechanism is to be treated as value of services and consequently service recipient (builder/contractor) is obliged to deduct income tax at source (TDS) on such service tax paid under reverse charge?
- In case where the works contract is allotted on 'inclusive of service tax' basis, whether service recipient is liable to pay service tax under reverse charge mechanism on such work contract?
- Whether service recipient (builder/contractor) can discharge service tax liability under reverse charge mechanism from accumulated Cenvat balance?
- Whether service provider (contractor or sub – contractor) discharging partial service tax liability is entitled to refund of Cenvat balance built up due to lower output tax liability and entitlement to full Cenvat?
- If Service provider (contractor) does not discharge his portion of tax liability under partial reverse charge mechanism, whether full tax can be recovered from service recipient (builder)?

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Words of Caution

- Views expressed are the personal views of faculty based on his interpretation of law
- Application/implications of various provisions will vary on facts of the case and law prevailing on relevant time
- Contents of this presentation should not be construed as legal or professional advice
- This is an educational meeting arranged with clear understanding that neither Faculty nor Mulund Study Circle will be responsible for any error, omission, commission and result of any action taken by participant or anyone on the basis of this presentation

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THANK YOU