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CHARTERED ACCOUNTANTS

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INDIRECT TAX REVIEW
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EXCISE

CUSTOMS

SERVICE TAX

VALUE ADDED TAX

Inside this edition

P.O.T. FOR SERVICES TAXABLE FROM OCTOBER 1, 2014

In terms of changes made to Section 66D of the Finance Act, 1994 read with Notification No.**18/2014-S.T** dated August 25, 2014, certain new services which were exempt, will come into the service tax net from 1-10-2014. Thus, space of space for advertisement other than in print media and services provided by radio taxis would be taxable from 1-10-2014. The pertinent question that arises is the point of taxation for these services rendered during the period prior to 1-10-2014.

It is relevant to refer to Rule 5 of the Point of Taxation Rules, 2011, one of the most mischievous rules that one comes across in the service tax law. This rule reads as under:

5. Payment of tax in case of new services.-

Where a service is taxed for the first time, then,-

(a) no tax shall be payable to the extent the invoice has been issued and the payment received against such invoice before such service became taxable;

(b) no tax shall be payable if the payment has been received before the service becomes taxable and invoice has been issued within fourteen days of the date when the service is taxed for the first time.

This amended Rule 5 which has come into effect from 1-4-2012 vide Notification No.**4/2012-ST** dated 17-3-2012 is bound to create big time confusion vis-à-vis the point of taxation in respect of the new services coming into the tax net with effect from 1-10-2014.

Consider these….

1. In terms of Sub-Rule (a) of Rule 5 reproduced above, service tax, in respect of a new service would have to be levied unless both the invoice and the payment against such invoice have been received by the service provider before the date such new service has come into effect.

This rule goes against the very foundation of the service tax law, which is now based on accrual basis as contrasted to the old law that existed before 01-04-2012 under which, the service provider was liable to pay service tax on the cash basis, i.e. on the basis of receipts. It is amazing that during the time that the Board came out with this notification **4/2012-ST**dated 17th March, 2012, the service tax law fastening tax liability on accrual basis had already come into effect. This makes one wonder as to the kind of confusion that prevails at the level of the Board.

Be that as it may……taking the example of the new services coming into effect from 1-10-2014 (eg. Sale of space for advertisement in non-print media), as per this Rule, the service provider would be liable to pay service tax in respect of invoices raised before 1-10-2014 and remaining uncollected as on 1-10-2014. It seems clear that Rule 5(a) of the POT Rules is*ultra vires* Section 66B of the Finance Act, 1994, inasmuch as, service tax liability under Section 66B can be levied only

on 'services provided or to be provided or agreed to be provided'. This Rule would travel beyond the charging section by fastening the tax liability on the service provider even though he has not rendered any services after the date of introduction of tax on the new services.

Moreover, the concept involving levy of tax and the concept involving collection of tax are two entirely different concepts. The pre-requisite for collection of tax is the levy of tax. TIOL readers would be familiar with the landmark decision of the Apex Court in *Collector of Central Excise, Hyderabad Vs. Vazir Sultan Tobacco Co. Ltd.* - 2002-TIOL-215-SC-CX-LB rendered in 1996, wherein it was held as under, in para 5:

"Once the levy is not there at the time when the goods are manufactured or produced in India, it cannot be levied at the stage of removal of the said goods. The idea of collection at the stage of removal is devised for the sake of convenience. It is not as if the levy is at the stage of removal; it is only the collection that is done at the stage of removal. Section 3(1) of the Central Excise Act says: "(1) There shall be levied and collected in such manner as may be prescribed duties of excise on all excisable goods other than salt which are produced or manufactured in India…."

The Apex Court further held as under, in Para 11, of this decision:

"The removal of goods is not the taxable event. Taxable event is the manufacture or production of goods"

If one applies the ratio of this decision to the service tax law, it is clear that, when there was no levy on the date of rendering of the service, service tax liability cannot be fastened on the service provider on the basis of the date of receipt of payment.

Moreover, the Apex Court, in its decision rendered on October 26, 2010, in *Association of Leasing and Financial Service Companies v. Union of India* - 2010-TIOL-87-SC-ST-LB has categorically held in Paras 18, 19 and 37 that, the taxable event, in respect of levy of service tax, is the "rendition of services". So, even on the basis of this binding decision, Rule 5 (a) would fall flat.

Before concluding…..

There is no issue in so far as Rule 5(b) of the POT Rules is concerned.

Nobody bothered about this Rule…. Now that, this is the first time new services are being subjected to the levy since this Rule came into the statute book, this Rule could see a judicial challenge in the days to come, for sure. Unfortunately, since this is the only direct rule that is applicable for new services, none of the other rules can be of help to the service providers.

CBEC would be well advised to issue a clarification on Rule 5(a), as otherwise, there is bound to be harassment to service providers, vis-à-vis the new taxable services coming into the tax net from 1-10-2014.

THE CENVAT CONUNDRUM

UNION Budget 2014 has brought far reaching changes in the availment of CENVAT Credit on inputs and input services. Some of the provisions can prove to be overly draconian as they aim to disallow CENVAT Credit which is an absolute and undeniable right of the assessees.

All excise and service tax assessees will have to make significant changes in invoice processing system and accounting entries in order to ensure that no CENVAT Credit goes unclaimed. The amendments are discussed below:

I. Amendment in CENVAT on input and input services:

Sub-rule (1) of Rule 4 of the CENVAT Credit Rules, 2004 lays down the conditions for availing CENVAT Credit on inputs. Similarly, sub-rule (7) of Rule 4 lays down the conditions for availing CENVAT Credit on input services.

In both the above sub-rules, the following proviso has been inserted:

"Provided also that a manufacturer or the provider of output service shall not take CENVAT Credit after six months of the date of issue of any of the documents specified in sub-rule (1) of Rule 9".

According to the above proviso, CENVAT Credit has to be availed within 6 months of the invoice date. **This proviso has come into effect from 1st September, 2014.**

This proviso will affect entities who do not process invoices within 6 months or those who pay advance to vendors and receive invoices which are 6 months old.

For example, *X Ltd*. has received an invoice in the month of August 2014 dated 01.08.2014 inclusive of service tax. *X Ltd*. is eligible to avail CENVAT Credit of the said service tax. However, the invoice processing chain in the company is long and there are frequent delays. As a result, the invoice which was dated in the month of August is entered in the books of accounts on 15.02.2015 i.e. in the month of February. In this case, 6 months have elapsed from the date of invoice and hence *X Ltd.* will not be able to avail CENVAT Credit of service tax on the invoice.

To avoid CENVAT Credit getting lapsed due to the above amendment, the assessee should make sure that CENVATABLE invoices when entered in the book of accounts are not more than 6 months old. In other words, invoices should be booked within 6 months of the date of invoice.

II. Amendment in CENVAT in case of Reverse Charge Mechanism:

The following provisos have been added in sub-rule (7) of Rule 4:

"Provided that in respect of input service where whole of the service tax is liable to be paid by the recipient of service, credit shall be allowed after the service tax is paid."

"Provided further that in respect of an input service, where the service recipient is liable to pay a part of service tax and the service provider is liable to pay the remaining part, the CENVAT Credit in respect of such input service shall be allowed on or after the day on which payment is made of the value of input service and the service tax paid or payable as indicated in invoice, bill or, as the case may be, challan referred to in rule 9."

According to the first proviso, **in case of full reverse charge** (i.e., when 100% service tax is to be paid by the service receiver), CENVAT Credit can be availed after the service tax has been paid. This means that in case of 100% reverse charge, CENVAT Credit of the service tax paid can be availed irrespective of whether the payment of value of service as mentioned in the invoice has been made or not. The availment of CENVAT Credit will be subject to amendment discussed in (I) above i.e., the CENVAT Credit of service tax paid on reverse charge will have to be availed within 6 months of the date of challan.

According to the second proviso, **in case of partial reverse charge**, for the portion of service tax which is collected by the service provider, CENVAT Credit can be availed by the service receiver after payment of value of invoice AND tax thereof. Whereas, for the portion of service tax which is discharged by the service receiver, the rule is silent as to when the CENVAT Credit can be availed. Taking an approach similar to full reverse charge, the CENVAT Credit of the latter portion should be availed after payment of tax.

III. Time limit for payment of invoice:

The following proviso has been added in sub-rule (7) of Rule:

"Provided also that in case the payment of the value of input service and the service tax paid or payable as indicated in the invoice, bill or as the case may be challan referred to in rule 9, except in respect of input service where the whole of the service tax is liable to be paid by the recipient of service, is not made within three months of the date of the invoice, bill or, as the case may be, challan, the manufacturer or the service provider who has taken credit on such input service, shall pay an amount equal to the CENVAT credit availed on such input service and in case the said payment is made, the manufacturer or output service provider, as the case may be, shall be entitled to take the credit of the amount equivalent to the CENVAT Credit paid earlier subject to the other provisions of these rules."

The above proviso will be applicable in case of input service and partial reverse charge (to the extent of service provider's invoice).As per the above proviso, payment of a CENVATABLE invoice should be made within 3 months. If the payment is not made within 3 months, then CENVAT credit availed on the basis of invoice will have to be reversed.

Clubbing the effect of this proviso and the proviso explained in (I) above, payment has to made within 3 months, failing which CENVAT Credit will have to be reversed. If the payment of the invoice is made within 6 months then CENVAT Credit can be availed back. **However, if the payment is not made within 6 months then the CENVATABLE invoice will become 6 months old and by virtue of the first proviso, CENVAT Credit available on that invoice will lapse forever.**

IV. In Nutshell:-

(i) CENVAT Credit on Inputs and Input Services:

To be availed within 6 months of invoice.

(ii) CENVAT Credit in case of 100% reverse charge:

To be availed after payment of tax (Value of invoice paid or not).

(iii) CENVAT Credit in case of Partial reverse charge:

To avail Credit on invoice of Service Provider (pay Tax and Value).

To avail Credit of ST paid on reverse charge (Rule silent) - interpretation- avail credit after payment of tax.

(iv) CENVAT Credit (except in case of 100% reverse charge):

Payment not made within 3 months (reverse CENVAT Credit).

Payment within 6 months (Take CENVAT again) - not beyond 6 months because then the invoice would be 6 months old and will be hit by (i) above.

Payment beyond 6 months - CENVAT lapses forever

V. Chart of CENVAT Credit Availment on Inputs and Input Services (w.e.f. 01.09.2014):-

Sr. No.	**Particulars**	**General**		**100% Reverse Charge**	**Partial Reverse Charge**		
					ST on invoice of SP		**ST paid on Reverse Charge**
(i)	When to avail	Within 6 months of Invoice date.		After Payment of Tax	After Payment of Tax and Value.		After Payment of Tax
(ii)	Whether Payment of Invoice made within 3 months	Yes	No	-	Yes	No	-
	Consequences	-	Reverse CENVAT Credit		-	Reverse CENVAT Credit	-
(iii)	Whether Payment of Invoice made after expiry of 3 months but before 6 months	Yes	No	-	Yes	No	
	Consequences:	Take CENVAT	CENVAT Credit	-	Take CENVAT	CENVAT Credit	

		Credit back which was reversed earlier	Lapses forever		Credit back which was reversed earlier	Lapses forever	

DEPUTATION OF EMPLOYEES – WHETHER AT ALL A SERVICE?

THE *department has been continuously striving to levy service tax on the deputation of employees, a common phenomenon amongst group entities whereby the employees of one Group Company are deputed to another Group Company and the salary/cost of such employees* **are** *reimbursed at actuals to the Group Company deputing the employee. Such attempt of the department has given rise to a number of disputes and consequently the judicial pronouncements on the subject. Still, the taxability of the transaction is not very clear particularly given the fact that all the judgements pertain to the pre-negative list based service tax regime.*

In order to effectually analyze the taxability of the said transaction under the current negative list based service tax regime, it would be pertinent to refer to the relevant provisions of the service tax statute. In the current regime, service tax is payable on all the services except those which are covered under the negative list or are specifically exempted from the levy of service tax. The term 'service' has been defined in Section 65B(44) of the Finance Act, 1994 as any activity carried out by a person for another for consideration but excluding certain specified activities. Provision of service by an employee to the employer in the course of or in relation to his employment has been stipulated as one such exclusion. Further, the term "supply of manpower" *is defined under Rule 2(1)(g) of the Service Tax Rules, 1994 as* supply of manpower, temporarily or otherwise, to another person to work under his superintendence or control.

While there would be no confusion in holding that deputation of employees by one Group Company to other Group Company would constitute an activity *undertaken by* one person for another, *the other issues regarding consideration, coverage of activity in the exclusion clause etc. are dealt with in the subsequent paragraphs.*

Given the above framework of provisions, let us analyze the judgements pronounced on the said subject to understand their relevance in the present context.

Recently, the Hon'ble Gujarat High Court in the case of CST vs. Arvind Mills Ltd. *- 2014-TIOL-441-HC-AHM-ST had an occasion to consider the taxability of deputation of employees in Group Company. In the said case, the respondent had deputed its employees in its group companies for undertaking some stipulated work for limited period, after which the employees were to be repatriated to the respondent. All throughout, the control and supervision over the deputed employees remained with the respondent. The actual cost incurred by the respondent in terms of salary, remuneration and perquisites was only reimbursed by the group companies on which service tax was demanded by the department under the category of 'manpower recruitment or supply agency service'.*

The Hon'ble High Court mainly relied on the definition of 'Manpower Recruitment or Supply Agency' as existed during the impugned period and held that the respondent cannot be said to be a 'commercial concern' engaged in providing the specified services and the subsidiary companies cannot be said to be its 'client'. Accordingly, in absence of the agency-client relationship, it was held that service tax would not be payable by the respondent on deputation of employees in the group companies.

Ratio of the above judgement may not come as an aid in the present context to take such transaction out of the purview of service tax where the service provider need not be a commercial concern and service recipient need not be his client.

Let us now refer to some other judgements wherein the leviability of such transaction was under challenge. In the case of Volkswagen India Pvt. Ltd. vs. Commissioner of Central Excise, Pune-I - *2013-TIOL-1640-CESTAT-MUM, the Appellant had employed some foreign nationals (called 'Global Employees') who were previously employed with other group entities. On their deputation in the Appellant Company, the said personnel were relieved by the other group companies and worked as whole time employees of the Appellant and were put at the disposal and exclusive control of the Appellant. However, the social security liability was discharged by the foreign company in the home country of the Global Employees which was reimbursed by the Appellant. The revenue argued that the same constitutes rendition of 'manpower supply or recruitment agency service' by the foreign holding company to the Appellant. To support its contention, the revenue submitted that after a period of 3-4 years, such global employees go back to the foreign company. The revenue further contended that the Appellant should have paid full salary directly to its employees rather than routing a part through the foreign company.*

However, the Appellant objected to the levy and submitted that the income earned by the global employees is treated as salary under the provisions of the Income Tax Act and that the Appellant has also issued necessary TDS Certificate in the capacity of an employer. The Appellant also submitted that merely because a part of the salary of global employees was paid in their home country through the holding company, it cannot be said that the foreign company has rendered services of supply of manpower to the Appellant. The Appellant also placed reliance on Circular No. 96/7/2007 wherein it has been clarified that in the case of supply of manpower, individuals are contractually employed by the manpower recruitment or supply agency and that the Employer-employee relationship in such cases exists between the agency and the individual and not between the individual and the person who uses the services of the individual.

The Tribunal accepted the submission of the Appellant and held that the global employees are working with the Appellant as their employees and accordingly, there is no supply of manpower service to the Appellant by the foreign company and that the method of disbursement of salary cannot determine the nature of transaction.

Similarly, in the case of Paramount Communication Ltd. vs. Commissioner of Central Excise, Jaipur - *2013-TIOL-37-CESTAT-DEL, the Appellant and its sister concern was utilizing the services of some common staff located in their common head office at Delhi who were*

on the payroll of the Appellant. The sister concern was reimbursing its share of cost to the Appellant on which service tax was demanded by the department under Manpower Recruitment or Supply Agency Service.

The Tribunal held that the Appellant is a manufacturer of excisable goods and is not engaged in the business of supply of manpower, though it was sharing the services of some of the personnel with its sister concern. Further, there is no case of supply of manpower by the Appellant to the sister concern as the employees continued to work for the Appellant also and arrangement in which certain employees work for two of the sister concerns and the expenses of employees are shared, the manpower is not supplied by one company to other. The service is by the personnel to two companies in question and not by one company to the other. So, no service is provided by the Appellant to its sister concern. The fact that payment to employee is made by one company and there is inter-company payment of the share of cost of the employees utilized by the other company cannot be interpreted to mean that one company was providing service to the other. *Some judgements have also been passed staying the recovery of tax on such transactions like in the case of* Bain & Company India Pvt. Ltd. vs. CST, Delhi - *2012-TIOL-138-CESTAT-DEL and* ITC Ltd. vs. Commissioner of Service Tax, New Delhi - *2012-TIOL-855-CESTAT-DEL.*

Though the above judgements again pertain to pre-negative list based service tax regime, the same may still be relevant given the fact that under the present context as well, services provided by the employee to the employer are kept outside the ambit of service tax net. Accordingly, in case it can be established that the deputed employee shares the employee-employer relationship with the company where he has been deputed, the same may take the transaction out of the service tax net. A number of indicatives may support the said relationship like issuance of employment letter by the company where the employee has been deputed, applicability of HR policy of such company to the deputed individual including those relating to his emoluments, appraisals, increments, promotions etc., treatment of amount reimbursed to the group company towards the salary cost of the deputed employee in the books of accounts, deduction of income tax u/s 192 (applicable to salaries) by such company etc. and may help the companies in avoiding the unwarranted litigation with the department. It may be noted that mere reimbursement of salary cost at actuals is not sufficient to exclude the transaction out of the purview of the service tax net as held by the Tribunal in the case of The Sanjivani (Takli) Sahakar iSakhar Karkhana Ltd. vs. Commissioner of Central Excise and Customs, Aurangabad - *2014-TIOL-355-CESTAT-MUM wherein it was held that the law does not envisage that the service provider should always render the service on profit basis. Even if loss is incurred in the provision of service, on the consideration received, service tax liability would accrue.*

However, it would be relevant here to refer to the draft Circular bearing F.No.354/127/2012-TRU dated 27-07-2012 wherein it has been clarified that the cases of secondment whereby certain staff belonging to an organization is placed at the disposal of a subsidiary company or any other associate company, the same would be covered by the definition of manpower supply as the contractual employment continues with the parent company. Though the said circular is still in the draft mode, the same shows the intent of the department of taxing such transaction and accordingly, the dispute by the department

cannot be totally ruled out. It would however be relevant to note that the said draft circular, in the case of joint employment where one entity pays the salary cost of the staff on behalf of the other joint employers which is later on recovered at actuals, clarifies that the same will not be liable to service tax being a mere cost reimbursement.

If we test the above draft circular in light of the provisions of law, it would be difficult to accept the clarifications provided by the said circular in view of their inherent contradiction. While on the one hand, the circular recognizes the principle that mere reimbursement of salary cost by one of the joint employers to other joint employer will not amount to rendition of the service, the said circular on the other hand attempts to hold the service tax leviability on reimbursement of salary cost of deputed employees by one group company to the other group company. While holding so, the Circular proceeds to assume that the contractual employment continues with the parent company. As stated above, in case the documentation as exemplified above shows that the deputed individual shares the employer-employee relationship with the company where he has been deputed, it may be argued that service tax would not be leviable.

However, till the time the CBEC does not remind itself of the need to clarify the position by issuance of a final circular or till the time any judgement is not pronounced on the subject under the current service tax regime, service tax leviability on the employee deputation would continue to puzzle the assessees.

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