

**WESTERN INDIA REGIONAL COUNCIL OF INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA**

**CENVAT ISSUES EMANATING FROM ABATEMENT, VALUATION AND CLASSIFICATION**

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**Day & Date : Saturday, 21<sup>st</sup> November, 2015**

**Preamble:**

WIRC has organized this workshop on indirect taxation for participants having reasonable or expert knowledge of Service tax. The purpose of this meeting is to discuss and deliberate on relating to Cenvat issues emanating from abatement, valuation and classification. Keeping in view the purpose of workshop and profile of participants, faculty will refrain from elementary discussion on service tax.

The paper consists of issues on brewing controversies in cenvat. These issues/ controversies might come up for testing by judicial forums at later date. There could be several dimensions to the issues raised and there could be many view points on such issues.

Faculty candidly admits that he is learning this complicated and ever evolving taxation law. The faculty would present his views on case studies/ issues to be best of his ability, knowledge and experience. The service tax authorities and/or Judiciary may or may not concur with faculty's views on the issues to be discussed.

The case studies/ issues are now put up for consideration and discussion:

**Services taxed at alternate rates and cenvat:**

**Case Study 1**

'A' is an IATA agent. He discharges service tax liability at 0.7 %of domestic basic fare and 1.4 % of basic international fare U/r 6(7) of Service Tax Rules, 1994.

He claims full cenvat of all its inputs, capital goods and input services. He has been advised that he is not entitled to full cenvat as he is not discharging service tax at full rate.

Is this advice correct?

Also opine whether service recipient is entitled to cenvat of service tax charged by IATA agent?

### **Abatement and cenvat:**

#### **Case Study 2**

M/s Vega bond tours is a reputed package tour operator having commenced business on 01.07.2012. It has been claiming abatement of 25% and discharging service tax liability on abated rate of 3.09% upto 31.03.2015 on its gross sales proceeds.

They were advised that they should first claim Cenvat of all input services and reverse 75% thereof as it relates to exempted portion of the service.

During the period 01.07.2012 to 31.03.2015, their net cenvat claim (25%) was Rs. 10 lacs. Their turnover for said period was Rs. 50 crores.

Kindly opine on correctness of above advice and adverse implications, if any.

#### **Case Study 3**

Mr. D is a builder constructing residential complex. During the F.Y. 2013-14, he has paid service tax on abated rate on booking advances received by it. He has claimed cenvat of Rs. 50 lacs on input services mainly consisting of works contract services provided by contractors, architect services, legal services, brokerage on sale of flats, etc. He also claimed cenvat on 'Capital goods'.

His accounts were covered under EA 2000 Audit by service tax authorities and following audit objections were raised:

- Abated service is an 'exempt service' u/r 2(e) of cenvat credit Rules, 2004 and hence Mr. D is not eligible for cenvat.
- Abatement of 75% (or 70%) of sales proceeds of flats covers construction material and land cost on which no service tax is paid by D and hence 75% (or 70%) of cenvat claimed should be reversed.

Kindly Advise and guide Mr. D

## Case Study 4

A Company provides railway containerized freight service w.e.f 01.04.2015.

Rail freight service is entitled to abatement subject to non-claiming of Cenvat credit. Company also pays substantial input service tax on freight charged by railway. Company has taken commercial call to pay service tax on full freight (not to claim abatement) and claim Cenvat credit of input service tax charged by railway on abated value of the freight.

Some clients do not get Cenvat of service tax charged on the freight and hence insist the company to charge service tax at abated rate.

### Issue under deliberation

- Whether company can discharge service tax liability on railway freight services partly on full rate and partly on abated rate?
- Once abatement is prescribed, is it compulsory for rail operator to claim abatement?
- Whether service tax authorities can deny abatement on rail freight under the pretext that it has claimed cenvat in respect of common services?

### Valuation and cenvat:

## Case Study 5

"M/s Rachana is a civil contractor engaged in construction of buildings.

Rachana was paying service tax under works contract service category at composition rate on the value of contracts. It was also claiming cenvat of input services and capital goods.

Their accounts for the period 01.04.2010 to 31.03.2015 were covered under EA 2000 Audit by service tax authorities and audit objection was raised that M/s Rachana has not paid service tax on material portion of the contract value and hence proportionate cenvat should be reversed.

Whether objection raised by Service Tax Authorities is legally tenable?

## Case Study 6

M/s Delicious Private Limited runs a restaurant and also undertakes outdoor catering contracts.

During F.Y. 2013-14, he has paid service tax on Restaurant and Outdoor catering sales. It has claimed cenvat of Rs. 50 lacs on input services.

Their accounts were covered under EA 2000 Audit by service tax authorities and following objection was raised:

- M/s Delicious Private Limited has not paid service tax on 60% of restaurant sales and 40% on outdoor catering sales and hence cenvat claimed should be reversed to that extent.

Whether objection raised by Service Tax Authorities is legally tenable?

## Case Study 7

M/s Elevators Limited engaged in manufacturing and installation of lift. It has following billing pattern and is discharging service tax liability till date as under:

Sale value of the lift	Rs. 30,00,000	Excise duty	Rs. 3,75,000
Installation contract (comprising of other materials)	Rs. 10,00,000	Service tax @ 5.60%	Rs. 56,000
<b>Total</b>	<b>Rs. 40,00,000</b>	<b>Total output tax</b>	<b>Rs. 4,31,000</b>
Payment to subcontractors for installation	Rs. 8,00,000	Service tax @ 5.60%	Rs. 44,800
		<b>Net tax incidence</b>	<b>Rs. 3,86,200</b>

Honorable Supreme Court in the case of M/s Kone Elevator India Private limited (2014-TIOL-57-SC-CT-CB) held that entire contract of Rs. 40,00,000 is a works contract.

In such a case, the tax incidence would be as under:

Assessable value of the lift	Rs. 30,00,000	Excise duty	Rs. 3,75,000
Installation contract (comprising of other materials)	Rs. 10,00,000	Service tax @ 5.60% on total contract value of <b>Rs. 40,00,000</b>	Rs. 2,24,000
<b>Total</b>	<b>Rs. 40,00,000</b>	<b>Total output tax</b>	<b>Rs. 5,99,000</b>
Payment to subcontractors for installation	Rs. 8,00,000	Service tax @ 5.60%	Rs. 44,800
		<b>Net tax incidence</b>	<b>Rs. 5,54,200</b>

The Elevator's Limited has been advised that based on the decision of Ahmedabad Tribunal in case of M/s. S V Jiwani (2014-TIOL-559-CESTAT-AHM) it is permissible to treat entire works contract as service and to pay service tax at full rate on entire contract value and claim Cenvat of excise duty paid on lift and also service tax on input services. The facts matrix in such case would be as under:

Assessable value of the lift	Rs. 30,00,000	Excise duty	Rs. 3,75,000
Installation contract (comprising of other materials)	Rs. 10,00,000	Service tax @ 14% on gross contract value of <b>Rs. 40,00,00</b>	Rs. 5,60,000
<b>Total</b>	<b>Rs. 40,00,000</b>	<b>Total output tax</b>	<b>Rs. 9,35,000</b>
Payment to subcontractors for installation	Rs. 8,00,000	Service tax @ 5.60%	Rs. 44,800
Excise duty paid on lift			Rs. 3,75,000
		<b>Net tax incidence</b>	<b>Rs. 5,15,200</b>

Whether above referred alternative is permissible?

## **Classification and Cenvat:**

### **Case Study 8**

A company intends to expand its production capacity. It has two options:

#### **Option A**

- To construct mezzanine floor in existing unit for storage of raw material and finished goods and install new machinery in space available.
- To Change Electrical and plumbing fittings of existing unit also to do electrical and plumbing installation on mezzanine floor.

#### **Option B**

- To construct additional floor on existing unit and install new machinery in said floor.
- To do electrical and plumbing fittings on the additional floor.

Kindly discuss the cenvat eligibility of:

- Construction and works contract service provided by civil contractors.
- Electrical and plumbing fittings services.