



Hospitality industry

Key indirect tax issues

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A close-up photograph of a person's hand holding a blue pen and writing on a document. The hand is positioned on the right side of the frame. In the background, a silver laptop is open, a calculator is visible, and a white coffee cup is on the left. The scene is set on a desk with a window in the background, suggesting a professional or office environment.

Key indirect taxes impacted

Key Indirect Taxes - Hotel Industry

Service tax	VAT	FTP, Customs & Excise	Other taxes
<ul style="list-style-type: none">▶ Room rentals▶ Restaurant services▶ Banquet services▶ Convention services▶ Club membership▶ Rent a cab services▶ Dry cleaning services▶ Health club/ Spa/ Beauty parlour services▶ Renting of immovable property▶ Internet services▶ Money changing services	<ul style="list-style-type: none">▶ Sale of food and beverages in restaurant(s)▶ Sale of food under banquet arrangements▶ Sale of goods from retail shops▶ In-room sales of food (such as in-room dining, mini bar, etc)	<ul style="list-style-type: none">▶ Customs duty payable on import of capital goods, motor cars, etc▶ Concessional customs duty rates under EPCG scheme▶ Duty credit scrips under SFIS▶ Central Excise on manufacture of bakery products▶ State Excise on alcoholic beverages	<ul style="list-style-type: none">▶ Luxury tax applicable on room rentals▶ Entertainment tax on casinos, discos, video game parlours, etc▶ Luxury tax and entertainment tax rates vary from State to State

Impact of indirect taxes

Indirect taxes have an impact on the following

- ▶ Applicability of multiple indirect taxes have an impact on the pricing of food and beverages, room tariffs, etc, thereby impacting the price competitiveness
- ▶ Eligibility to claim credit / set off of taxes have an impact on the cost effectiveness
- ▶ Burden of compliance under various indirect tax legislations
- ▶ Ambiguities on taxability and credit eligibility on various transactions



Service tax

Service tax – key taxable services

Restaurant services

Particulars	From 1 May 11 to 31 March 2012	From 1 April 2012 to 30 June 2012	From 1 July 2012 to 31 March 2013	From 1 April 2013
Scope	Restaurants having AC and liquor license	Restaurants having AC and liquor license	Restaurants having AC and liquor license	Restaurants having AC
Abatement	70%	70%	60%	60%
Effective rate	3.09%	3.708%	4.944%	4.944%
CENVAT credit	No credit on inputs, input services and capital goods	No credit on inputs, input services and capital goods	Credit not permitted on inputs under chapters 1 to 22	Credit not permitted on inputs under chapters 1 to 22

Service tax – key taxable services

Outdoor catering services

Particulars	Upto 31 March 2012	1 April 2012 to 30 June 2012	From 1 July 2012 onwards
Abatement	50%	50%	40%
Effective rate	5.15%	6.18%	7.416%
CENVAT credit	No credit on inputs, input services and capital goods	No credit on inputs, input services and capital goods	Credit on inputs, input services and capital goods available except inputs under chapters 1 to 22 (food stuffs, consumables, etc)

Service tax – key taxable services

Hotel accommodation services

Particulars	Upto 31 March 2012	1 April 2012 to 30 June 2012	From 1 July 2012 onwards
Abatement	50%	50%	40%
Effective rate	5.15%	6.18%	7.416%
CENVAT credit	No credit on inputs, input services and capital goods	No credit on inputs, input services and capital goods	Credit on inputs services available No credit on inputs and capital goods

Service tax – key taxable services

Other key services provided by hotels

Services	Service tax rate
Rent a cab services	40% abatement (rate – 7.416%)
Health & fitness services	12.36%
Fitness centre services	12.36%
Internet café services	12.36%
Cleaning services	12.36% (prior to 1 July 2012 only dry cleaning was taxable)
Renting of shops in the hotel premises	12.36%



VAT

VAT – key taxable transactions

Transaction	Maharashtra VAT rate
Sale of food	12.5%
Sale of non alcoholic aerated beverages	20%
Sale of alcoholic beverages	20%
Sale of non aerated non alcoholic beverages (mineral water, juices, etc)	12.5%
Sale of Spa products	12.5%
Sale of cigarettes	20%
Sale of food in composite packages	Rule 59 - Taxable turnover shall be: - 5% - where charges which include breakfast - 15% - where charges which include breakfast and lunch - 30% - where charges which include breakfast, lunch and dinner



Central Excise

Central Excise – key taxable transactions

Transaction	Central Excise duty rate
Food preparations prepared or served in a hotel, restaurant or retail outlet	Exempt from Central Excise duty
Cakes, pastries & cookies prepared by the hotel	6.18%
Chocolates prepared by the hotel	12.36%



Luxury tax

Luxury tax – key taxable transactions

Transaction	Maharashtra luxury tax rate
Room tariff – payable on actual tariff (not declared tariff)* -Exceeding Rs 1,200 per day per room -Rs 200 - 1,200 per day per room -Tariff up to Rs 200 per day per room	10% 4% Nil
Other services provided in a hotel including charges for air-conditioning, television, radio etc if charges exceed Rs 200 per day per room	10%
Services provided to consulate/foreign diplomats	Exempt from luxury tax
Telephone, laundry, valet, courier, photo copy, fax, etc	Not regarded as luxury– based on a circular

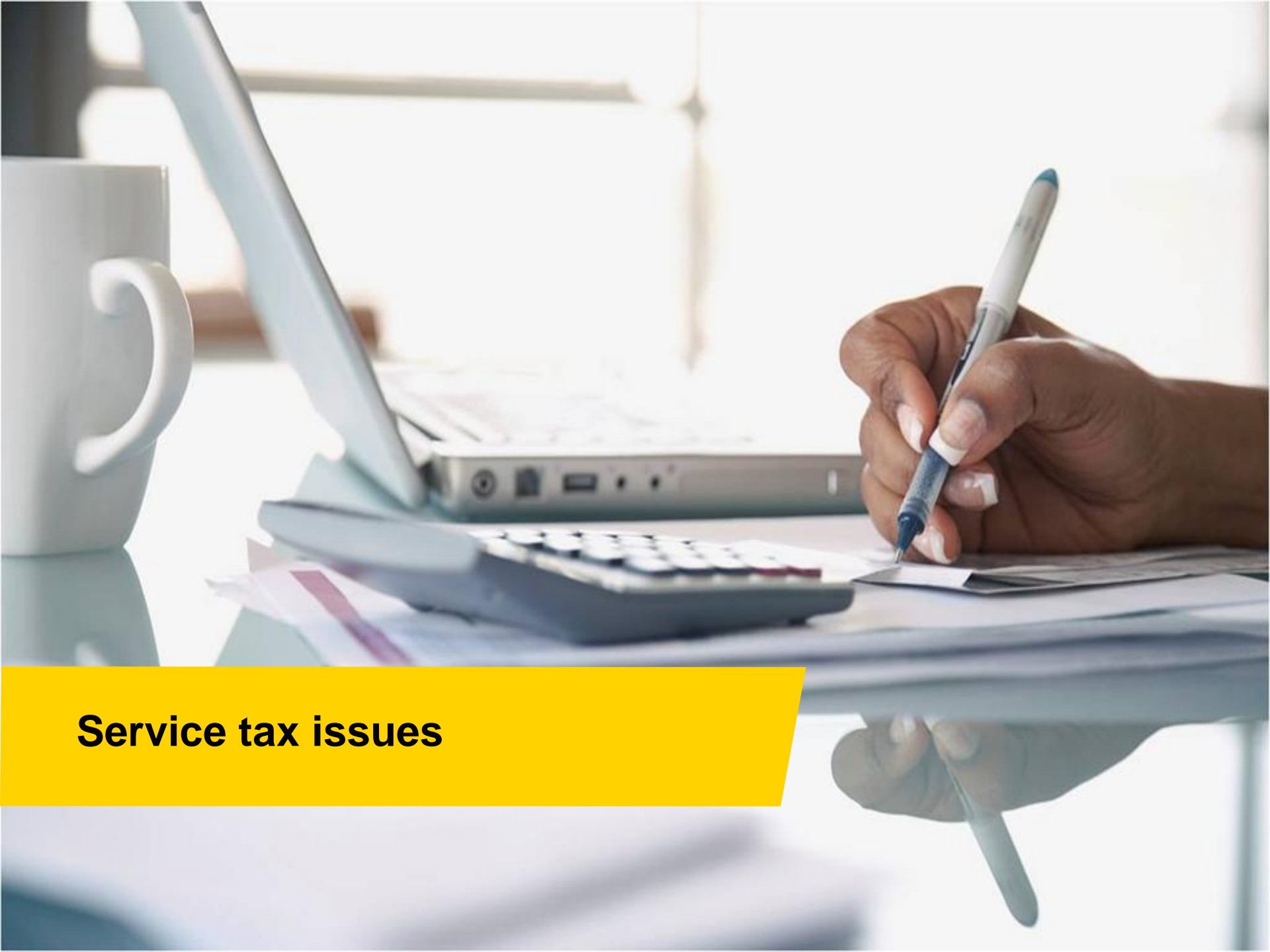
**In some states such as Delhi, luxury tax is payable on declared tariff and not actual tariff.*



Case study

Case study – computation of indirect taxes

Transaction	Service tax	VAT	Luxury tax	Effective tax
Room Tariff Rs 9,000 covering only accommodation	$9,000 * 12.36% * 60\% = 667.44$	Not applicable	$9,000 * 10\% = 900$	17.42%
Room Tariff Rs 10,000 including breakfast	$10,000 * 12.36% * 60\% = 741.6$	$10,000 * 5% * 12.5\% = 62.5$	$10,000 * 10\% = 1,000$	18.04%
Dining at a restaurant having AC Rs 1,000	$1,000 * 12.36% * 40\% = 49.44$	$1,000 * 12.5\% = 125$	Not applicable	17.44%
Supply of food in a convention with total charges of Rs 2 lacs	$Rs\ 2\ lacs * 12.36% * 70\% = Rs\ 17,304$	$Rs\ 2\ lac * 12.5\% = Rs\ 25,000$	Not applicable	21.15%
Outdoor caterer with total charges of Rs 2 lacs	$2\ lacs * 12.36% * 60\% = Rs\ 14,832$	$2\ lacs * 12.5\% = Rs\ 25,000$	Not applicable	19.92%



Service tax issues

Restaurants / supply of food – service tax issues

- ▶ Taxing entry:
 - ▶ (zzzzv) to any person, by a restaurant, by whatever name called, having the facility of air-conditioning in any part of the establishment, at any time during the financial year, which has licence to serve alcoholic beverages, in relation to serving of food or beverage, including alcoholic beverages or both, in its premises
- ▶ Post Negative List, the exemption reads:
 - ▶ 19. Services provided in relation to serving of food or beverages by a restaurant, eating joint or a mess, other than those having (i) the facility of air-conditioning or central air-heating in any part of the establishment, at any time during the year, and (ii) a licence to serve alcoholic beverages;
- ▶ Rule 2C of Valuation Rules
 - ▶ 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 (or as a part of outdoor catering)

Restaurants / supply of food – service tax issues

- ▶ Is service tax applicable on ‘service charges’ charged by restaurants?
 - ▶ Clarified in TRU Circular dated 25 April 2011 - service charge to be included
- ▶ Whether service tax applies on ‘take away’ parcels provided by restaurants?
 - ▶ Customers do not use restaurant’s facilities while ordering food or collecting parcels – no clarification on this aspect
- ▶ Is service tax applicable on counters at theatres?
- ▶ Is service tax applicable on self service restaurants?
 - ▶ TRU circular dated 28 February 2011 that mere sale of goods is not a service
 - ▶ Supreme Court in of K Dharmodharanswamy Naidu held that value cannot be split and VAT applies on entire amount charged in a restaurant
- ▶ Is service tax applicable on food supplied by office canteens?
 - ▶ Exemption available only to serving food or beverages by a restaurant, eating joint or a mess, other than those having air-conditioning / central air-heating facility
- ▶ Can service tax be levied on value including VAT?

Restaurants / supply of food – service tax issues

- ▶ Is service tax applicable on mini bar consumption?
 - ▶ Argument could be adopted that mini bar consumption is a pure sale of goods and does not involve any sale of goods – hence should not attract service tax
- ▶ Sky Gourmet - is it sale or service?
 - ▶ LSG Sky Chefs v. CST (2009) 19 STT 440 and 25 STT 10 (CESTAT)
- ▶ Supreme court in Tamil Nadu Kalyan Mandapam while upholding service tax on outdoor catering services made a clear distinction from restaurants where choices or "service" is fairly limited
- ▶ Delhi High Court in IRCTC case held that there is no service in catering inside a train as there is no choice or service provided - once the food is loaded onto the train, it is sold
- ▶ However, Kerala High Court in Saj Flight Services held that supply of goods and beverages to aircrafts falls under outdoor catering services
- ▶ Services are provided by air port lounges?
- ▶ Entertainment combined with food?

Restaurant/ catering services – valuation issue

- ▶ It appears that Valuation Rule 2C is not optional but to be followed mandatorily
- ▶ Issue for caterers who charge separate amounts for sale of F&B and for services and where value charged for services is substantially lower than 60% of total amount charged
 - ▶ Impact on the Airline catering industry
- ▶ Some arguments in favor of valuation on basis of actual amounts:
 - ▶ If value of service is clearly ascertainable, service tax should be levied on actual value - Valuation Rules triggered only if value of services not ascertainable
 - ▶ Based on Guidance note, the legislative intent appears to be only to address the difficulty normally arising in determining the value of service portion
 - ▶ Section 67 provides that value of services is the gross amount charged for services – Section 67 should override Rules

In-room dining services

- ▶ Up to 1 July 2012 – Specific clarification in Circular 139/8/2011 - TRU dated 10 May 2011 that
 - ▶ When the food is served in the room, service tax cannot be charged under the restaurant service as the service is not provided in the premises of the air-conditioned restaurant with a licence to serve liquor
- ▶ With effect from 1 July 2012, in room dining may qualify as a taxable service since its not specifically covered under negative/ exempt list
- ▶ Rule 2C of Valuation Rules allows valuation of service portion in any activity involving supply of food, drink, etc in a restaurant at 40% of total amount charged
 - ▶ May not apply to in-room dining
 - ▶ No other specific valuation rule regarding in-room dining

Issues - CENVAT Credit reversal computation

Restaurant services

Position post 1 July 2012

- ▶ "exempted service" means *a taxable service whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken*
 - ▶ Services not covered under abatement scheme
 - ▶ 40% of total amount charged is deemed to be value of services as per Valuation Rules
 - ▶ Services may not qualify as exempted services
 - ▶ CBEC's Guidance Note states that sale of food in restaurants is clearance of exempted goods and Rule 6 of CENVAT Credit Rules would be applicable to such clearances
- ▶ **Whether restaurant services should be considered as exempt services?**
 - ▶ **If yes, whether the deemed portion of food and beverages sold ie 60% or full amount ie 100% should be considered as exempted turnover?**
 - ▶ **If no, whether still Cenvat reversal is required?**

Hotel accommodation - Bundled Services

- ▶ Taxing entry:
 - ▶ (zzzzw) to any person by a hotel, inn, guest house, club or campsite, by whatever name called, for providing of accommodation for a continuous period of less than three months
- ▶ Post Negative List, the exemption reads:
 - ▶ 18. Services by way of renting of a hotel, inn, guest house, club, campsite or other commercial places meant for residential or lodging purposes, having declared tariff of a unit of accommodation below rupees one thousand per day or equivalent
- ▶ Valuation:
 - ▶ 70% in case of bundled service by way of 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 other place, specially arranged for organizing a function) together with renting of such premises
 - ▶ 60% if only renting

Hotel accommodation - Bundled Services

- ▶ Defined as provision of one type of service with another type or types of services
- ▶ If services are bundled in the ordinary course of business
 - ▶ The bundle of services will be treated as consisting entirely of such service which determines the dominant nature of such a bundle
- ▶ If services are not bundled in the ordinary course of business
 - ▶ The bundle of services will be treated as consisting entirely of such service which attracts the highest liability of service tax
- ▶ Whether the services are naturally bundled in the ordinary course of business or not needs consideration
- ▶ It is crucial to determine correct nature of services to ascertain place of provision of service

Hotel accommodation - Bundled Services

Hotel accommodation package with breakfast / dinner, etc

- ▶ Presently classifiable under 'accommodation services' and abatement from value of services is claimed
- ▶ Whether such services could be classified as naturally bundled services of accommodation
- ▶ CBEC's Education guide clarifies that hotel accommodation gives essential character to the bundle & should, therefore, be treated as service of providing hotel accommodation
- ▶ Accordingly, Hotel accommodation package with meals should be eligible for 40% abatement from value of services

Hotel accommodation - Bundled Services

Bouquet of services covering accommodation, conference, biz. centre, etc

- ▶ For eg – where hotel is booked for a conference on lump sum package with following facilities:
 - ▶ Accommodation for delegates
 - ▶ Breakfast and one meal for delegates,
 - ▶ Tea and coffee during conference
 - ▶ Availability of conference room
 - ▶ Business centre services
- ▶ Where the service is described as convention service, it is able to capture the entire essence of the package - Service may be regarded as convention service
- ▶ However, hotel may also charge individually for the services as long as there is no attempt to offload the value of one service on to another service that is chargeable at a concessional rate

Issues - CENVAT Credit reversal computation

Accommodation services

- ▶ As Per Rule 6(3) of CENVAT Credit Rules, credit attributable to exempted services is required to be reversed by service provider
- ▶ Reversal amount = CENVAT credit availed * (Exempt Turnover) / (Total turnover)
- ▶ Exempted turnover includes exempted goods as well as exempted services

Position prior to 1 July 2012

- ▶ Entire turnover of accommodation services & restaurant service required to be considered as exempt services for calculation of reversal amount, if abatement scheme applied

Issues - CENVAT Credit reversal computation

Accommodation services

Position after 1 July 2012

- ▶ Services for which part value is taxable, are covered in definition of 'exempted services' only if no credit permitted on inputs as well as input services
- ▶ For accommodation services, credit of input services, capital goods as well as specified inputs is available even under abatement scheme

- ▶ Should accommodation services be considered as exempt services?
- ▶ If yes, whether exempted portion ie 40% or full amount ie 100% to be considered as exempted turnover?

Other service tax issues

Loyalty program

- ▶ Customers avail services such as accommodation, dining, etc by redeeming reward points – whether service tax applicable on such amounts?
- ▶ Typically in such cases, customers does not pay to the hotel, however the hotel receives amounts equivalent to points redeemed from the loyalty program manager

Booking cancellation charges

- ▶ Amounts received from the loyalty manager should typically be regarded as consideration for services received
- ▶ If the hotel recovers cancellation charges from customers for booking cancellation – whether service tax should be applicable?
 - ▶ Definition of service includes any activity done for a consideration.
 - ▶ Blocking rooms / reservations for guests could be regarded as an activity

Other service tax issues

- ▶ Paid outs – on guest's demand, hotels arrange for facilities such as doctor on call, baby sitter, nurses, etc – where hotel recovers these charges from guests at cost (without mark up) – whether service tax is applicable
- ▶ If the hotel recovers cancellation charges from customers for booking cancellation – whether service tax should be applicable?
 - ▶ Definition of service includes any activity done for a consideration.
 - ▶ Blocking rooms / reservations for guests could be regarded as an activity



VAT

VAT – key issues

- ▶ Article 366(29A) (f)
 - ▶ a tax on the 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,
 - ▶ and such transfer, delivery or supply of any goods
 - ▶ shall be deemed to be
 - ▶ a sale of those goods by the person making the transfer, delivery or supply and
 - ▶ a purchase of those goods by the person to whom such transfer, delivery or supply is made;

VAT – key issues

No abatements provided

- ▶ Service tax law provides for abatements in case of services such as accommodation, restaurant, banquet, outdoor caterer, etc
- ▶ However, under the VAT laws, typically there are no abatements ie VAT is payable on total amount charged
- ▶ This results in the same amounts being charged to both service tax and VAT

Banquet arrangements – valuation

- ▶ Where amounts are charged on lump sum basis, VAT authorities have issued notices seeking to levy VAT on the entire value
- ▶ DDQ in the case of Tiptop Enterprises that in case of banquet arrangements, VAT is payable on the lump sum amount charged

VAT – key issues

VAT on service charge recovered by restaurants

- ▶ Whether VAT is applicable on service charges recovered by restaurants?
- ▶ As per definition of ‘sales price’, any sum charged by seller in respect of the goods at the time of or before delivery is to be included in the definition of sales price

Loyalty program

- ▶ Customers avail services such as dining, purchase of merchandise, etc by redeeming reward points – whether VAT applicable on such amounts?
- ▶ Typically in such cases, customers does not pay to the hotel, however the hotel receives amounts equivalent to points redeemed from the loyalty program manager
- ▶ Is VAT applicable on mini bar consumption?

VAT – key issues

Accommodation packages with meals

- ▶ Certain states such as Maharashtra have specific provisions for valuation of meals –Rule 59
- ▶ In other states, such as Delhi, no specific provisions for valuation of goods – what should be the basis of valuation? Should value be based on similar meals provided to other customers?
- ▶ Whether VAT is applicable on sale of food to employees at discounted rates?
- ▶ Where food / beverages are provided by air port lounges to members, free of charge, airline company pays the air port lounge – whether VAT applicable on such goods provided ?
- ▶ Whether VAT is applicable on complimentary food, mineral water , beverages supplied during conferences?

VAT – key issues

- ▶ Whether VAT is applicable on sale of food at the oil rigs located in high seas?
- ▶ Based on certain judgments, sale within 12 nautical miles liable to VAT

VAT – airline catering industry

- ▶ Scenario 1: Sale of F&B to airline companies at the port of origin – premium airlines
 - ▶ transaction typically regarded as a local sale in the state where goods are sold.
For eg: In case of Mumbai – Delhi flight, MVAT applicable on goods sold to F&B
- ▶ Scenario 2: Sale of F&B on Buy on Board ('BoB') basis – low cost airlines
 - ▶ Airline acts as an agent of the air line caterer and sells ready to serve meal to passengers
 - ▶ At the time of handing over of meal to Airline, it is not certain that the meal will be ultimately sold to passengers or will be returned back
 - ▶ Whether such transaction would attract VAT / CST given that sale takes place in mid air – if yes, whether local sale or inter state sale
- ▶ DDQ iby Andhra Pradesh VAT authorities in the case of Sky Gourmet that
 - ▶ any sale that takes place after commencement and before termination of interstate movement falls under Section 3(b) of the CST legislation
 - ▶ If aircraft travels from one state to another, CST should be applicable
 - ▶ If aircraft travels within the state (say Mumbai to Pune), MVAT should apply

Composite supplies – Multiple levies

- ▶ Various transactions (eg - banquets, conferences, restaurant services etc) attract multiple levies – VAT/ Service tax/ Luxury tax
- ▶ Different legislations contain different definitions for the taxable base

Key issue:

- ▶ Inclusion of one tax for purposes of computing taxable base for another – for eg – whether service tax to be included to compute luxury tax on room rentals?
- ▶ Different options available under various service categories such as mandap keeper, hotel accommodation services, restaurant services, etc for payment of Service tax
 - ▶ Option 1: Service tax on total amount charged less abatement at prescribed percentages with no CENVAT credit
 - ▶ Option 2: Payment of service tax on value charged for provision of services only
- ▶ Similarly schemes available under VAT legislations also (such as composition scheme)

Key issue:

- ▶ Optimization of indirect tax costs and credits – cost benefit analysis required



Key challenges & planning avenues

Key indirect tax challenges

- ▶ Multiplicity of taxes
- ▶ No uniformity in taxes across States
- ▶ Cascading of indirect taxes due to lack of credits across taxes
- ▶ Burden of compliance under various indirect tax legislations
- ▶ Ambiguities on taxability and credit eligibility on various transactions
- ▶ CENVAT credit restrictions on taxes paid on construction of hotels

Planning avenues to be explored

Construction of hotels

- ▶ Optimization of service tax and VAT cost - 'general scheme' vis-à-vis 'composition scheme'
- ▶ Exploring contract structuring options for EPC contracts in order to optimise indirect tax costs for the Project Owner
- ▶ Use of tax efficient structures such as in-transit sale, high sea sale, etc
- ▶ Issuance of Form C by Hotel for inter-state purchase of capital goods – permissibility to be examined
- ▶ CENVAT credit vs. Depreciation – cost benefit analysis

Export Promotion Capital Goods ('EPCG') scheme

- ▶ Import of capital goods at 3.09% (0% with effect from April 2013) subject to fulfillment of export obligation and other conditions.
- ▶ Special provisions allowing hotels to import motor vehicles for hotel operations under EPCG – custom duty on motor vehicles typically more than 100%.

Planning avenues to be explored

Served From India Scheme ('SFIS')

- ▶ Duty credit of 10% of free foreign exchange earned which can be used for payment of custom / excise duties on procurement of capital goods, office furniture & consumables
- ▶ Special provisions allowing hotels to import consumables including food items and alcoholic beverages against SFIS duty credit

State level incentives

- ▶ Fiscal benefits to hotel projects under State tourism policies
 - ▶ Key objective - high investments and employment generation
- ▶ Customized benefits possible for mega investment projects. Typical fiscal incentives include:
 - ▶ Stamp duty exemption on purchase/ lease of land
 - ▶ Luxury tax exemption for specified number of years (5 - 7 years)
 - ▶ Exemption from entertainment tax for specified number of years
 - ▶ Electricity duty concessions

Planning avenues to be explored

Ongoing operations

- ▶ Cost benefit analysis of service tax payable and credit available under abatement scheme v/s normal scheme
- ▶ Exploring the possibility to claim CENVAT credit on certain goods such as furniture, electronics, air conditioners, etc used by hotels
- ▶ Unbundling services i.e. split consideration wherever possible to avoid double taxation
- ▶ In cases where there is pure supply of food (and food not served) – to explored whether position can be taken that service tax is not applicable



Thank you

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