

SEMINAR ON CRITICAL ISSUES IN INCOME TAX & SERVICE TAX

SERVICE TAX ON BUILDERS & DEVELOPERS SERVICE TAX ON WORKS CONTRACT SERVICE: SCOPE OF LEVY, VALUATION & EXEMPTION

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TAXATION ON WORKS CONTRACT **INCLUDING CONSTRUCTION SERVICE**

1. Taxability

- 1.1. Section 66E of the Finance Act, 1994 provides for list of declared services wherein clause (h) of the above section provides that the **service portion** in the execution of a works contract is made liable to service tax.
- 1.2. Thus, services element in a works contract is liable to tax

2. What is “works contract”

- 2.1. Works contract means a contract wherein
 - transfer of property in goods involved in the execution of such contract and
 - 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 movable or
 - immovable property or
 - for carrying out any other similar activity or a part thereof
 - in relation to such property.

- 2.2. It is to be noted that in respect of movable property, only repair, maintenance, renovation, alteration is taxable. Any original work or any work other than those mentioned above in respect of movable property is not under coverage of service tax.



3. Valuation

- 3.1. Value of service portion in the execution of a works contract shall be
 - equivalent to gross amount charged for works contract
 - less value of transfer of property in goods involved in execution of said works contract and
 - less VAT/Sales Tax.
- 3.2. Value of works contract service shall include, -
 - labour charges for execution of the works;
 - amount paid to a sub-contractor for labour and services;
 - charges for planning, designing and architect's fees;



- charges for obtaining on hire or otherwise, machinery and tools used for the execution of the works contract;
- cost of consumables such as water, electricity, fuel used in the execution of the works contract;
- cost of establishment of the contractor relating to supply of labour and services;
- other similar expenses relating to supply of labour and services; and
- profit earned by the service provider relating to supply of labour and services

3.3. In case VAT or Sales Tax is paid on actual value of transfer of property in goods involved in execution of works contract, then such value adopted for payment of VAT to be taken as value of transfer of property for determining the value of works contract service as referred above.

3.4. If the value of service portion in the execution of a work contract has not been determined as above, then the person liable to pay service tax shall determine the service tax payable as under:

Works Contract	Service tax payable on
Execution of original works [#]	40% of the total amount [*] charged for the works contract
Maintenance or repair or reconditioning or restoration or servicing of any goods	70% of the total amount [*] charged for the works contract
Works contract, not covered above, including maintenance, repair, completion and finishing services such as glazing, plastering, floor and wall tiling, installation of electrical fittings of an immovable property	70% ¹ of the total amount [*] charged for the works contract

“original works” means

- all new constructions;
- all types of additions and alterations to abandoned or damaged structures on land that are required to make them workable;
- erection, commissioning or installation of plant, machinery or equipment

¹ Substituted for 60% w.e.f. 1st October 2014 by Notification No. 11/2014-ST dated 11th July, 2014.



* **“total amount”** means

- the sum total of the gross amount charged for the works contract **and**
- the fair market value of all goods and services supplied in or in relation to the execution of the works contract,
- whether or not supplied under the same contract or any other contract,
- after deducting-
 - the amount charged for such goods or services, if any; and
 - the value added tax or sales tax, if any, levied thereon:
- The service provider has to discharge service tax liability on fair market value for the works contract. If the amount of works contract is not at fair market value, then such fair market value has to be arrived at by generally accepted accounting principles.
- However, there are no accounting standards/ principle prescribed by ICAI to derive such fair market value.

3.5. CENVAT credit of duties or cess paid on any inputs shall not be taken, which are used in or in relation to the said works contract. However, CENVAT credit of duties or cess paid on Capital Goods and Input Service shall be available

4. Builder’s and Developer’s

4.1. Taxability

Section 66E of the Finance Act, 1994 provides for list of declared services wherein clause (b) of the above section provides that;

- 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
- is liable to service tax.

Hence service portion in sale of any commercial or residential or any other property is leviable to service tax.

CBEC has clarified vide its press release dated 26th October, 2015 that in areas under the jurisdiction of Municipal Corporation of Greater Mumbai i.e. Brihanmumbai Municipal Corporation (BMC), sale of flats/dwellings etc., where the entire consideration is received after issue of Occupancy



Certificate (OC) by BMC, leading to a mere transfer of title in immovable property, it would fall outside the definition of “Service” provided in Section 65B (44) of the Finance Act, 1994, and is therefore, not taxable

4.2. Abatement

- As the above value of above transaction includes value of goods, value of land and value of service, abatement to Builder’s and Developer’s has been provided vide Notification No. 26/2012-ST dated 20th June, 2012 to bring parity for taxing the transaction.
- Vide entry no. 12 of the said notification, abatement of 75% was provided in respect Construction of complex, building, civil structure or part thereof intended for a sale to a buyer subject to the condition;
 - Cenvat credit of Inputs has not been taken
 - Value of land in included in the amount charged from service receiver.
- W.e.f. 1st March, 2013 the rate of abatement was reduced from 75% to 70% in respect to high-end residential construction where carpet area exceeds 2000 sq.ft. **and** value charged exceeds Rs. 1 crore and in respect of Civil Construction.
- Now w.e.f. 8th May, 2013 rate of abatement of 70% has been set high-end residential construction where carper area is equal to or greater than 2000 sq.ft **or** value charged is equal to or greater than Rs.1 Crore.
- The summary of the above is provided below;

Description	% of Abatement
Construction of Residential units having carpet area of less than 2000 square feet and where the amount charged is less than Rs. 1 Crore	75%
Construction of Residential units having carpet area of 2000 or more than 2000 square feet or where the amount charged is Rs. 1 Crore or above	70%
Any other construction including commercial and industrial	70%



5. Exemptions

In negative list regime most of the exemptions are part of one single mega exemption notification vide Notification no. 25/2012 –Service Tax, Dated 20th June, 2012. These Exemptions became effective from the 1st July 2012. Below are the exemptions available in respect of work contract service and Constructions services.

5.1. **Services in relation to erection, construction, commissioning, installation, completion, fitting out, maintenance, repair, alteration or renovation provided to government / Local authority/ governmental authority [S. No. 12].**

5.1.1. Services provided to the Government or local authority/ governmental authority by way of erection, construction, commissioning, installation, completion, fitting out, maintenance, repair, alteration or renovation of –

- A. [a civil structure or any other original work meant predominantly for a non-industrial or non-commercial use or any other business or profession]²;
- B. a historical monument, archaeological site or remains of national importance, archaeological excavation, or antiquity specified under Ancient Monuments and Archaeological Sites and Remains Act, 1958 (24 of 1958);
- C. [a structure meant predominantly for use as (i) an educational, (ii) a clinical, or (iii) an art or cultural establishment]³;
- D. canal, dam or other irrigation works;
- E. pipeline, conduit or plant for (i) water supply (ii) water treatment or (iii)sewerage treatment or disposal; or
- F. [a residential complex predominantly meant for self-use or the use of their employees or other persons specified in the Explanation 1 to clause 44 of section 65 B of the said Finance Act]⁴

Governmental authority⁵ means an authority or a board or any other body;

² Omitted by Notification No. 6/2015-ST w.e.f. 1st April, 2015

³ Omitted by Notification No. 6/2015-ST w.e.f. 1st April, 2015

⁴ Omitted *ibid*



- (i) Set up by an Act of Parliament or a State Legislature; or
 - (ii) Established by Government,
- with 90% or more participation by way of equity or control,
To carry out any function entrusted to a municipality under article 243W of the Constitution.

5.2. Services in relation to construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration w.r.t. certain services used by public at large [S. No. 13].

5.2.1. Services provided by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration of,

- A. road, bridge, tunnel, or terminal for road transportation for use by general public;
- B. a civil structure or any other original works pertaining to a scheme under Jawaharlal Nehru National Urban Renewal Mission or Rajiv Awaas Yojana
- C. building owned by an entity registered under section 12 AA of the Income tax Act, 1961(43 of 1961) and meant predominantly for religious use by general public;
- D. pollution control or effluent treatment plant, except located as a part of a factory; or
- E. a structure meant for funeral, burial or cremation of deceased

5.2.2. Remark

5.2.2.1. The maintenance services provided w.r.t. services mentioned in (c) to (e) above was taxable till 30th June, 2012. Now the above entry exempt all the above said services provided.

5.2.2.2. In case of Roads, earlier, construction of all roads was excluded till 30th June, 2012. However the mega exemption exempts services in respect of

⁵ Amended vide Notification 2/2014-ST dated 30-1-2014. Prior to that defined as "governmental authority" means a board, or an authority or any other body established with 90% or more participation by way of equity or control by Government and set up by an Act of the Parliament or a State Legislature to carry out any function entrusted to a municipality under article 243W of the Constitution.



road used by general public only. Thus any of the aforesaid services in relation to road in a residential complex or a factory, etc. will attract service tax.

5.2.2.3. Construction, repair, etc. of non commercial building such as schools, college, hospitals, charitable clinic, etc. was not leviable to service tax till 30th June, 2012. The mega exemption does not cover the above service.

5.3. Services in relation to erection, commissioning, installation, construction, w.r.t. certain specified purposes [S. No. 14].

5.3.1. Services by way of erection, construction, commissioning and installation of original works pertaining to,-

- A. [~~airport, port or~~]⁶ or railways including monorail or metro;
- B. single residential unit otherwise than as a part of a residential complex;
- C. low- cost houses up to a carpet area of 60 square metres per house in a housing project approved by competent authority empowered under the 'Scheme of Affordable Housing in Partnership' framed by the Ministry of Housing and Urban Poverty Alleviation, Government of India;
- D. post- harvest storage infrastructure for agricultural produce including cold storages for such purposes; or
- E. mechanised food grain handling system, machinery or equipment for units processing agricultural produce as food stuff excluding alcoholic beverages;

The term "single residential unit" means a self-contained residential unit which is designed for use, wholly or principally, for residential purposes for one family.

5.3.2. Scenario prior to 1st July, 2012 in respect of above said services

5.3.2.1. Services in respect of airport, port and railways were all together excluded from the ambit of service tax by way of specific exclusion from the definition.

5.3.2.2. Services in respect of construction of complex services were exempt from service tax if the complex was having 12 or less units. The definition also excluded complexes used for personal use.

⁶ Omitted by Notification No. 6/2015-ST w.e.f. 1st April, 2015



5.3.3. Remark

- 5.3.3.1. Till 30th June, 2012 services as specified in clause (a), constructions other than original work, repairs, alteration, restorations and maintenance was not leviable to tax. However under mega exemption the said services are taxable.
- 5.3.3.2. In respect of services mentioned in clause (b) - A millionaire using the services for construction of a bungalow for himself will not pay service tax whereas a common man buying a under construction flat which is not approved by competent authority empowered under the 'Scheme of Affordable Housing in Partnership' framed by the Ministry of Housing and Urban Poverty Alleviation, Government of India/ having an area of more than 60 square meters even if approved by the above mentioned authority in a building having more than one unit will have to pay service tax.
- 5.3.3.3. Earlier construction of residential complex / building having less than 12 units were not leviable to service tax. Now, only those unit having an area of less than 60 square meters approved by competent authority empowered under the 'Scheme of Affordable Housing in Partnership' framed by the Ministry of Housing and Urban Poverty Alleviation, Government of India are only exempt and it does not matter if the unit is less than 12 units and more than one unit.

5.4. **Service provided by specified persons [S. No. 29(h)].**

- 5.4.1. Services by Sub-contractor providing services by way of works contract to another contractor providing works contract services which are exempt.

6. Issues:

- 6.1. Reliable Limited offers works contract services to clients across India. Standard terms of the contract Reliable Limited executes with clients contains a clause for retention of certain percentage of the total contract value. The retention amount is in the nature of security towards the quality of goods and services provided by Reliable Limited. Typically the contracts provide for payment of the retention amount after a specified period (usually one to three years) from the date of completion of job.



Reliable Limited raises for gross amount including the retention amount and service tax on entire bill. Reliable Limited has sought your opinion on the point of taxation of the retention amount.

- 6.2. Whether flooring work, plastering, painting, glazing, carpentry, plumbing, interiors etc., done during the course of construction can be considered as original works for valuation purposes and pay tax on 40%?

In above case, service was completed as on 30th September, 2014. However, invoice has been issued in October 2014 and payment has been received in November 2014. What shall be the value on which service tax is payable?

- 6.3. Mr. Karodpati has purchased a flat from M/s Chalu Developers Ltd. Mr. Karodpati has specifically requested the developers to use Italian Marble in his flat instead of usual Kadappa Stones. The Italian Marble shall be supplied by Mr. Karodpati to the Developer.

The developer has sub-contracted the work of tiling to M/s Tilers Ltd. In terms of request of Mr. Karodpati, the developer has instructed M/s Tilers Ltd. to fix Italian Marble in the respective Flat. The Italian Marble shall be supplied by Mr. Karodpati to the developer, who shall then give the same to M/s Tilers Ltd. Cement and other material for fixing of tile shall be supplied by M/s Tilers Ltd. What shall be value chargeable to service tax on the transactions?



- 6.4. Whether service tax is leviable on one time deposit taken by developers from flat buyers to pay for Municipal Taxes, water charges, Repair & maintenance of building etc before formation of CHS and such deposits are later transferred to CHS?

- 6.5. M/s Redevelopers Ltd. is redeveloping Aashiana C.H.S. Ltd. having 24 flats, each measuring 500 sq.ft. Under the agreement with society, M/s Redevelopers are given right to redevelop the society totaling to 25000 sq.ft. Out of the above space, 24 flats each measuring 625 sq.ft (2 BHK), totaling to 15000 sq.ft. shall be constructed by M/s Redevelopers for members of society and M/s Redevelopers shall sell the balance flats to outside Parties. M/s Redevelopers shall also pay to each member Rs. 50,000 as one time relocation charges, Rs. 30,000/- per month as Rent Compensation, Rs. 10 lacs to each member of Aashiana C.H.S. Ltd as lump sum compensation. Further M/s Redevelopers shall also pay Rs. 1 Crore to the Aashiana C.H.S. Ltd towards corpus of the society. Now what shall be the service tax liability of;

1. M/s Redevelopers Ltd.
2. Each Member of Aashiana C.H.S. Ltd
3. Aashiana C.H.S. Ltd (for corpus contribution received)

- 6.6. In the above case, M/s Redevelopers Ltd. has given an offer to the each of the 24 residents of Aashiana C.H.S. Ltd for buying extra space of 60 sq.ft (half room) for Rs. 18,000/- per sq.ft instead of market rate of Rs. 20,000/- per sq.ft. If the residents want to buy further 40 sq.ft (one full room), then they



shall have to pay Rs. 18,000/- per sq.ft for 60 sq.ft and Rs. 20,000/- per sq.ft. for remaining 40 sq.ft.

10 residents have opted to buy additional 60 sq.ft. whereas 2 residents have opted to buy additional 100 sq.ft.

In such scenario, what shall be the value on which M/s Redevelopers Ltd shall charge service tax to such residents?

6.7. M/s Kanjus Developers Ltd is engaged in construction of luxurious residential apartments. He is paying service tax on 30% of agreement value for booking received before completion certificate. He has sub-contracted the entire construction work to a contractor, who is charging service tax on 40% of contract value. M/s Kanjus Developers Ltd is also incurring various other expenditure in the project. He wants to know whether he is eligible to take CENVAT credit of service tax paid on following services

- Architect Service
- Works Contract Service (contractor)
- Legal Services (Lawyers for agreement drafting, etc.)
- Machinery Hire
- CA Service (Audit)
- Telephone at site/ sales office, etc.

6.8. M/s Kanjus developer completed its project of 100 residential flats and applied for Occupation Certificate in BMC. The Occupation Certificate was issued finally for the project on 15th January, 2016. Before issuance of OC, 85 flats have been sold and remaining 15 flats have been sold after OC.



M/s Kanjus Developer has availed total CENVAT of Rs. 40 crore on this project and out of that CENVAT balance of Rs. 5 crore is still available for utilization. M/s Kanjus Developer wants to discharge service tax liability of Rs. 2.5 crore towards flats booked from 1st January, 2016 to 14th January, 2016 from the CENVAT balance. Pls advise whether he can pay the said liability from his CENVAT balance?

6.9. M/s Builders Ltd. have hired security guards for their construction site from Mr. Chowkidaar. For services rendered in March and Invoices raised by 31st March 2015, service provider already charged 25% of ST amount. Payment of Invoice done in April 2015 and thereafter. What is the service tax liability of M/s Builders Ltd.?

6.10. Whether the construction of three floor house by contractor is leviable to service tax?

6.11. M/s Gharwale Ltd. is engaged in business of developing empty plots and building complex of bungalows on such plots. They are owners of plot of approx 9000 sq.ft. They have sub-divided the entire plot in 9 equal parts, each measuring 1000 sq. ft on which they plan to construct single bungalows on 8



plots and remaining 1 plot would be dedicated towards common play area. The entire complex would be having common water supply and sewage system. Whether such bungalows would be termed as single residential units or would they be part of a residential complex? Whether any exemption is available to M/s Gharwale Ltd.

6.12. M/s ABC Transporters are engaged in road transport of heavy machinery and equipment. Such machinery and equipment cannot enter cities through conventional routes due to space constraints at 'toll nakas' at outskirts of city. Accordingly, they obtain permission from local authorities for constructing a 'by-pass road'. Such permission is given subject to the condition that once the machinery/equipment passes through the bypass road, such bypass road shall be taken over by the local authority and made open for use by general public. Now, ABC Transporters has given contract for construction of such by-pass road to M/s Mazboot Sadak Co. Ltd. ABC Transporters seek your opinion whether service tax shall be leviable on service provided by M/s Mazboot Sadak Co. Ltd?

6.13. Ishwar Charitable Trust is an entity registered under section 12AA of the Income Tax Act. The Trust is contemplating construction of a Hospital for welfare of public at large. The layout the hospital includes a Temple in the premises. Now the Trust seeks your opinion on the leviability of service tax on construction of Hospital and Temple within the premises of Hospital.



6.14. M/s Reliable Constructors Ltd. have been awarded the composite contract in respect of construction of Mumbai Metro. Following is the scope of work of M/s Reliable Constructors Ltd.

- Piling Work and Construction of Pillars
- Erection and Installation of pre-fabricated concrete slabs
- Laying of tracks and overhead wiring on tracks
- Construction of Station
- Floor and wall tiling of Station, installation of electrical fittings in station

Whether service tax is leviable on the above work? If yes, on which portion of the works contract.

6.15. In the above work, M/s Reliable Constructors Ltd sub-contract the tiling and finishing work in respect of the Metro Station to M/s Tilers Ltd. The subcontract is also a composite contract. Whether service tax is leviable on Reliable Constructors Ltd. in respect of the Construction work of Mumbai Metro. Also whether service tax is leviable on service provide by M/s Tilers to M/s Reliable Constructors Ltd.?

6.16. What would be the answer in above case if M/s Tilers Ltd. are directly awarded the composite contract for tiling from Mumbai Metro?



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