
SEMINAR ON SERVICE TAX ON CONSTRUCTION INDUSTRY

On

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At

Khimji Kunverji Vikamsey Auditorium,

ICAI Tower,

Mumbai 400 051

Prepared by

CA Manish Gadia

Organised By:



WIRC of ICAI

TOPICS COVERED

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1. Background of Works Contract Service

1.1 Taxability

1.1.1 'Declared Service' includes certain services which may not be purely service but deemed to be a service within the framework of service tax provisions.

1.1.2 'Declared Service' has been defined under section 66E of the Finance Act, 1994, 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.

1.1.3 Thus, services element in a works contract is liable to tax.

1.2 What is "works contract"

1.2.1 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. Background on Construction Service (Builder's and Developer's)

2.1 Taxability

2.1.1 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.

3. Abatement

- 3.1 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.
- 3.2 **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.
- 3.3 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.
- 3.4 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.
- 3.5 The summary of the above is provided below;

| Nature | Carpet Area | Gross Amount Charged | % of Abatement | | |
|--------------------------|-------------|----------------------|----------------|-----------------------|---------------|
| | | | Upto 28/2/13 | From 1/3/13 to 7/5/13 | W.e.f. 8/5/13 |
| Residential | <2000 | <1 Crore | 75% | 75% | 75% |
| Residential | <2000 | >1 Crore | 75% | 75% | 70% |
| Residential | >2000 | <1 Crore | 75% | 75% | 70% |
| Residential | >2000 | >1 Crore | 75% | 70% | 70% |
| Commercial or Industrial | Irrelevant | | 75% | 70% | 70% |

4. 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.

4.1 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].

4.1.1 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;
- 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;
- 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.

Governmental authority¹ means an authority or a board or any other body;

(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.

4.2 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].

4.2.1 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

4.2.2 Remark

4.2.2.1 The maintenance services provided w.r.t. services mentioned in (c) to (e) above was taxable. It has now exempt all the above said services provided.

¹ 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

4.2.2.2 In case of Roads, earlier, construction of all roads was excluded. However the mega exemption exempts services in respect of road used by general public. Thus any of the aforesaid services in relation to road in a residential complex or a factory, etc. will attract service tax.

4.2.2.3 Earlier construction, repair, etc. of non commercial building such as schools, college, hospitals, charitable clinic, etc. was not leviable to service tax. The mega exemption does not cover the above service.

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

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

- A. airport, port 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.

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

4.3.2.1 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.

4.3.2.2 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.

4.3.3 Remark

4.3.3.1 Earlier in respect of 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.

4.3.3.2 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 having 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.

4.3.3.3 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.

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

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

5. **PRINCIPLES OF INTERPRETATION – SECTION 66F**

5.1 Sub-section 3 is a novel concept of "bundled service". It applies where two or more services are bundled together in the ordinary course of business or not in such

ordinary course of business. In the former case, it is described as “naturally bundled service” and in such case it shall be treated as provision of single service which gives such bundle its essential character. If two or more services are not naturally bundled, all the services shall be treated as provision of single service which results in the highest liability of service tax.

5.2 Bundled service is defined as a bundle of provision of various services wherein an element of provision of one service is combined with an element or elements of provision of any other service or services.

5.3 Two rules have been prescribed for determining the taxability of such services in sub-section (3) of Section 66F. These provisions are subject to provisions of rule contained in sub-section (2) of S. 66F.

5.4 **Naturally bundled service:**

5.4.1 The rule is, ‘If various elements of a bundled service are naturally bundled in the ordinary course of business, it shall be treated as provision of a single service which gives such bundle its essential character’. For example:

In certain cases, builders/developers charge additional amount known as “floor rise charges” in addition to the normal sale price of a flat since the construction cost increases as per the increase in the floor. Since the floor rise charge are recovered on account of additional construction cost it would be treated as part of the consideration for sale of flat in terms of provisions of section 66F (Naturally Bundled service).²

5.5 **Services which are not naturally bundled:**

5.5.1 The rule is, if various elements of a bundled service are not naturally bundled in the ordinary course of business, it shall be treated as provision of a single service which attracts the highest amount of service tax.

5.6 **Manner of determining if the services are bundled in the ordinary course of business:**

² Clarification F.No. V/ST-I/Tech-II/463/11 dated 31.08.2012 issued by Commissioner of Service Tax, Mumbai-I.

5.6.1 This would depend upon the normal practice followed in the business. Such practice adopted in the business can be ascertained from the terms of the contract, perception of the recipient of service, the nature of various services in the bundle, the prevailing practice of majority service provider in a particular business and such other factors. Other illustrative indicator would be that there is a single price the consumer pays for a package, or the elements are normally advertised as a package, or where the different elements are not available separately and they are integral to one or overall supply that if one or more is removed from that, the nature of supply would get affected. However, no straight jacket formula can be laid down and each case has to be individually examined.

5.7 **Determination of taxability of “composite transactions”:**

5.7.1 The manner of treatment of such composite transaction wherein an element of provision of service is combined with an element of sale of goods for the purpose of taxation.

6. POINT OF TAXATION

6.1 **General rule:** Earlier the payment of service tax was only when there was receipt of payments. Now, w.e.f. 1st April, 2011 or 1st July, 2011, as the case may be, point of taxation shall be:

A. Where the invoice for the service provided or agreed to be provided is issued within 30/45 days of the date of completion of provision of services the Point of Taxation shall be earliest of the following dates:

- (i) Date of issue of invoice
- (ii) Date of receipt of payment

B. Where the invoice for the service provided or agreed to be provided is not issued within 30/45 days of the date of completion of provision of services the Point of Taxation shall be earliest of the following dates:

- (i) Date of completion of provision of services
- (ii) Date of receipt of payment.

6.2 Completion of service³: Clarification on 'completion of service' is issued clarifying that completion of service would include not only the physical part of providing the service but also the completion of all other auxiliary activities that enable the service provider to be in a position to issue the invoice. Such auxiliary activities could include activities like measurement, quality testing, etc which may be essential pre-requisites for identification of completion of service. The test for the determination whether a service has been completed would be the completion of all the related activities that place the service provider in a situation to be able to issue an invoice. However such activities do not include flimsy or irrelevant grounds for delay in issuance of invoice.

6.3 Continuous Supply Of Services

6.3.1 A 'continuous supply of service' has been defined to mean – [Rule 2(c)]

- any service provided or to be provided continuously **or on recurrent basis** by a service provider under a contract for a period more than 3 months; or
- such services which the Central Government prescribes by a notification to be in the nature of continuous supply of services.

Note: Services on recurrent basis would mean services which are provided on recurring basis and are not continuous in nature. Services provided by a Courier Agency would be considered as provided on recurrent basis wherein the said courier agency collects the courier at regular intervals from their clients.

6.3.2 Specified *services under continuous supply*: the provision of following taxable services shall be treated as continuous supply of service irrespective of the period of service provision contract i.e. even if the contract for service provision is less than 3 months then also following services shall be considered as continuous supply of service till 30th June, 2012:

- Commercial or Industrial Construction [Sec 65(105)(zzq)]
- Residential Complex Construction Services [Sec 65(105)(zzh)]
- Telecommunication Services [Sec 65(105)(zzx)]
- Internet Telecommunication Services [Sec 65(105)(zzu)]
- Works Contract Services [Sec 65(105)(zza)].

W.E.F. 1st July, 2012 following services shall be considered as continuous

³ Circular No. 144/13/ 2011 – ST dated 18.07.2011

supply of service:

- Telecommunication Services, and
- Service portion in execution of Work Contract

6.3.3 However, in case of 'continuous supply of service' the general rule would be applicable subject to the following modifications:

- where in terms of the contract the provision of the whole or part of the service is determined periodically on the completion of an event; and
- Such event obligates payment by the service receiver, the date of completion of each such event shall be the ***date of completion of provision of services.***

6.3.4 Illustrations:

| Date of Part Completion of Service as specified in contract | Date of Receipt of Payment | Date of Bill | ST Liability arises in | Remarks |
|-------------------------------------------------------------|-----------------------------|------------------------------|------------------------|------------------------------------------------------------------------------------------------------|
| 5 th July 2013 | 2 nd August 2013 | 27 th July 2013 | July 2013 | Since Invoice is issued within 30 days, Issue of Invoice or Receipt of payment, whichever is earlier |
| 5 th July 2013 | 27 th July 2013 | 2 nd August 2013 | July 2013 | Since Invoice is issued within 30 days, Issue of Invoice or Receipt of payment, whichever is earlier |
| 5 th July 2013 | 2 nd August 2013 | 16 th August 2013 | July 2013 | Since the invoice is issued after 30 days, the date of whole or part completion of service |

7. ADJUSTMENT OF TAXES PAID

7.1 ADVANCE PAYMENT OF SERVICE TAX [Rule 6(1A)]

From 1st March, 2008 facility of advance payment of service tax has been introduced and available to all the assessees.

The assessee who is paying service tax in advance should follow the following procedures:

- Intimate to the jurisdictional Superintendent of Central Excise within 15 days of such payment.

- Service tax paid in advance is allowed to be adjusted against service tax liability for the subsequent period. It is sufficient that such adjustment is disclosed in the periodical return to be filed.

7.2 ADJUSTMENT OF EXCESS SERVICE TAX PAID [Rule 6(3), 6(4A), 6(4B) and 6(4C)]

Service not wholly of partly provided or amount is renegotiated: Where an assessee has issued an invoice, or received any payment, against a service to be provided which is not so provided by him either wholly or where the amount of invoice is renegotiated due to deficient provision of service, or any terms contained in a contract, the assessee may take the credit of such excess service tax paid by him, if the assessee.-

(a) has refunded the payment or part thereof, so received for the service provided to the person from whom it was received; or

(b) has issued a credit note for the value of the service not so provided to the person to whom such an invoice had been issued.

It has been clarified that in such cases of adjustment the assessee is required to file the details in respect of such *suo motu* adjustments done by him at the time of filing the service tax returns (Para 21.1 of Trade Notice No. 7/98-Service tax dated 13.10.1998 issued by Commissioner of Central Excise, Mumbai-I). Along with enclosure of documentary evidence for adjustment of such excess service tax paid. It is to be noted that rule 6(3) does not allow adjustment of excess payment of service tax *per se*, say due to clerical mistake etc. In such cases the assessee has to follow the procedure laid down in section 11B of Central Excise Act to claim the refund of excess tax paid.

Self adjustment of excess tax paid: Self-adjustment of excess service tax paid by assesseees is allowed subject to the following conditions:

- (i) Self-adjustment of excess credit is allowed on account of reasons other than interpretation of law, taxability, valuation or applicability of any exemption notification.

- (ii) Adjustment of excess paid service tax without any monetary limit⁴.
- (iii) Adjustment can be made only in the succeeding month or quarter.
- (iv) No intimation required⁵.

8. Recent Issues in Service Tax

8.1 M/s Strong Constructors have been awarded a contract for construction and maintenance of canal (for the purpose of supply of drinking water) by Canal and Irrigation Co Ltd. (wholly owned by Govt. of Gujarat). The contract has been awarded on 01.12.2013. Whether service tax is leviable on the same?

A similar contract was also awarded to M/s Strong Constructors by Canal and Irrigation Co Ltd. on 01.03.2014. Whether service tax is leviable on the same?

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8.2 M/s ABC Transporters are engaged in road transport of heavy machinery and equipments. 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?

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⁴ Prior to 1st April, 2012, Excess amount paid and proposed could have been adjusted upto Rs.200,000⁴ for the relevant month or quarter

⁵ Prior to 1st April, 2012, the details of self-adjustment had to be intimated to the Superintendent of Central Excise within a period of 15 days from the date of adjustment.

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8.3 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.

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

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8.5 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.

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8.6 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.

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8.7 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.?

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8.8 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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8.9 M/s Welders & Co. Ltd. is engaged in the business of providing welding services for large scale projects. They have been recently engaged by Pipeline Ltd. for welding pipeline being laid throughout India for transport of Oil. The terms of contract between Welders & Co. Ltd and Pipeline Ltd. state that Welders shall have to get an X-Ray done of the joints welded by them and obtain certificate that work is as per specification. Pursuant to this, Welders shall be eligible for payment. Now, Welders & Co. Ltd. finished the actual welding job on 20th April, 2014. They obtained required certification on 3rd June, 2014 and then raised invoice on 25th June, 2014. They seek your opinion with respect to the Point of Taxation.

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8.10 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 invoice 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.

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8.11 XYZ Ltd. are have been given the contract of construction of a commercial building by M/s. Kanjus Ltd. The terms of the contract specify the quality of material to be used, time limit for completion of contract, design specification. Now, after completion of contract, M/s. Kanjus Ltd. has demanded a renegotiation and asked price to be reduced to 85% of original contract value since the building design is not as per his specification and also that the work was completed 6 months after deadline. XYZ Ltd. had already raised RA Bills for 90% of the contract amount and paid service tax accordingly. They seek your opinion on adjustment on excess paid service tax on account of renegotiation by M/s Kanjus Ltd.

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