

REVERSE CHARGE MECHANISM AND POINT OF TAXATION



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Reverse Charge Mechanism-Basics

- Generally the liability to pay service tax for provision of a service is cast on the service provider.
- However, in case of **certain specified services**, the responsibility of **paying** the service tax is cast on the service receiver. This legal jargon is called '**Reverse Charge Mechanism**'. This exception to the general rule is provided under section 68(2) of the Finance Act, 1994 (the Act)
- Threshold exemption of Rs Ten Lakh is not available to the service receiver.
- CENVAT Credit cannot be utilised for payment of service tax under Reverse Charge.

Reverse Charge Mechanism (Brief History)

- Reverse charge mechanism was first introduced in 1997 by shifting the onus from providers to receivers vide section 68(2) of the Act read with Rule 2(1)(d) of the Service Tax Rules in case of:
 - Clearing and forwarding agent's service
 - Goods transport operator's service
- Liability on recipients of these two services was fixed merely by introducing the said machinery provisions in Rule 2(1)(d) of the Rules, it was challenged.
- Supreme Court Decision in the case of **Laghu Udyog Bharati & Anr. vs. UOI & Others** 1999 (112) ELT 365 (SC) / 2006 (2) STR 276 (SC)-
*“Rule 2(d)(xii) and (xvii) of the Rules (as it prevailed then) in so far as it makes the persons other than the clearing and forwarding agents or goods transport operators responsible for collecting service tax were **ultra vires the Finance Act, 1994** itself and such sub-rules were accordingly struck down”.*

Reverse Charge Mechanism (Brief History)

- The charging section 66 of the Act itself was amended.
- Certain services were notified vide Notification No.36/2004-ST dated 31/12/2004 – Recipient liable to pay entire tax amount.
- With effect from 18/04/2006, section 66A was introduced in the Act creating a charge of service tax on a person receiving taxable services in India provided by a person from a country other than India, the person receiving such services was made liable for service tax.
- The **Bombay High Court's decision** in the case of Indian National Shipowners' Association vs. UOI 2009 (13) STR 235 (Bom) and **upheld by the Supreme Court** in 2010 (17) STR OJ57 (SC), *held to the effect that only from the date of the introduction of section 66A, service tax liability could be fastened on the recipients located in India for the services received from outside India.*

Reverse Charge Mechanism

Taxable Services notified (Brief History)

- Notification No.30/2012-ST issued on 20/06/2012 with effect from 01/07/2012. – various services are notified - Partial reverse charge taxation also introduced with effect from 01/07/2012.
- Section 68(2) of the Act is the applicable provision whereby reverse charge i.e. liability to pay service tax is fastened on the recipient of a service. Section 68 (2) is reproduced below

*“Notwithstanding anything contained in sub-section (1), in respect of **such taxable service** as may be **notified** by the central government in the official gazette, the service tax thereon shall be paid by **such person** and in **such manner** as may be prescribed at the rate specified in section 66B and all the provisions of this chapter shall apply to such person as if he is the person liable for paying the service tax in relation to such service”*

**Persons liable under Reverse Charge vis-à-vis notified services under section 68(2)
[vide Notification No.30/2012-ST read with Notification No.45/2012-ST dated 07/08/2012,
Notification No.10/2014-ST dated 11/07/2014 and Notification 7/2015 dated 01/03/2015]**

Sr.No	Notified Taxable Service	Service Provider (SP)	Service Receiver (SR)	Rate (SP)	Rate (SR)
1	Insurance Agent Service	Insurance Agent	Person carrying on insurance business	NIL	14%
2	Recovery Agent Service	Recovery Agent	Banking Company, Financial institution or a non-banking financial company	NIL	14%
3	Aggregator Service (w.e.f. 01/03/2015)	Services provided involving an aggregator	Aggregator or person representing the Aggregator	NIL	14%
4	Transportation of goods by road	Goods Transport Agency	Factory, Registered Society, Co-operative Society, Dealer of Excisable Goods, Body Corporate, Partnership firms [including LLP]	NIL	4.2% [14% * 30%]

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Persons liable under Reverse Charge vis-à-vis notified services under section 68(2) of the Act

Sr.No	Notified Taxable Service	Service Provider (SP)	Service Receiver (SR)	Rate (SP)	Rate (SR)
5	Sponsorship Service	Any	Body Corporate or Partnership Firm	NIL	14%
6	Advocate Service	Individual/Firm/LLP and Arbitral Tribunal	Business Entity	NIL	14%
7	*Support Services provided by Government or Local Authority [Except Renting of Immovable Property and sub-clause (i), (ii) and (iii) of sub clause (a) of section 66D of the Act.	Government or Local Authority	Business Entity	NIL	14%

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Persons liable under Reverse Charge vis-à-vis notified services under section 68(2) of the Act

Sr.No	Notified Taxable Service	Service Provider (SP)	Service Receiver (SR)	Rate (SP)	Rate (SR)
8	Services by a Director	Director of a company or a body corporate	Company or Body Corporate	NIL	14%
9	Mutual Fund Agent or Distributor Service (w.e.f. 01/04/2015)	Mutual Fund Agent or Distributor	Mutual Fund or Asset Management Company	NIL	14%
10	Selling or marketing agent service (w.e.f. 14/05/2015)	Selling or marketing agent	Lottery Distributor/Selling Agent	NIL	14%

Persons liable under Reverse Charge vis-à-vis notified services under section 68(2) of the Act

Sr.No	Notified Taxable Service	Service Provider (SP)	Service Receiver (SR)	Rate (SP)	Rate (SR)
11(a)	Rent-a-cab service *at abated rate	Individual/H UF/ Partnership firm	Business Entity registered as a Body Corporate	NIL	5.6% (14%*40%)
11 (b)	Rent-a-cab service *non abated rate	Individual/H UF/ Partnership firm	Business Entity registered as a Body Corporate	7% (14%* 50%)	7% (14% * 50%)
12	Supply of manpower and security service	Individual/H UF/ Partnership firm	Business Entity registered as a Body Corporate	NIL	14%

Persons liable under Reverse Charge vis-à-vis notified services under section 68(2) of the Act

Sr.No	Notified Taxable Service	Service Provider(SP)	Service Receiver(SR)	Rate (SP)	Rate (SR)
13	Works Contract Service (Original Works)	Individual/H UF/ Partnership firm	Business Entity registered as a Body Corporate	2.8% (14%*40%*50%)	2.8% (14%*40%*50%)
13(a)	Works Contract Service (Others)	Individual/H UF/ Partnership firm	Business Entity registered as a Body Corporate	4.9% (14%*70%*50%)	4.9% (14%*70%*50%)
14	Import of Services	Provider in a non-taxable territory	Receiver in Taxable Territory	NIL	14%

INSURANCE AGENCY SERVICE (Sr.No. 1 of 30/2012-ST)

- 100% service tax payable by the **person carrying on insurance business** in respect of services provided by an **insurance agent**
- **Exemptions contained in the Mega Exemption Notification (ME)**
ME:26 Services of general insurance business provided under various schemes viz. Hut Insurance, Cattle Insurance, Pradhan Mantri Suraksha Bima Yojana etc.
ME:26A Services of life insurance business provided under various schemes viz. Varishtha Pension Bima Yojana, Pradhan Mantri Jeevan Jyoti Bima Yojana etc.

AGGREGATOR SERVICES (Sr.No.3 of 30/2012-ST)

(W.E.F. 01/03/2015)

- **Aggregator is defined under the Service Tax Rules, 1994**

*‘(aa); “aggregator” means a person, who owns and manages a **web based software application**, and by means of the application and a **communication device**, enables a potential customer to connect with persons **providing service** of a particular kind under the **brand name or trade name of the aggregator**.*
- **3 parties involved in an aggregator model**
 - a) The Aggregator
 - b) Service Provider using the brand name or trade name of the Aggregator
 - c) Customer
- The liability to discharge service tax is on the aggregator under Reverse Charge Mechanism. It is also provided that if the aggregator does not have presence in the taxable territory, the person representing the aggregator shall discharge the liability or the aggregator shall appoint a person for discharging the tax liability.

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GOODS TRANSPORT AGENCY (Sr. No.4 of 30/2012-ST)

- Section 65B(26) of the Act:- Any person who provides service **in relation to** transport of goods by road and **issues a consignment note.**
- **Service Receiver:- Person liable for paying the freight is:**
Factory, Registered Society, Co-operative Society, Registered Dealer under Central Excise Act, 1944, Body Corporate and Partnership Firm, AOP.
- **Notification No. 26/2012-ST:** Value of Taxable Service-30% (Provided CENVAT Credit on inputs, input services and capital goods is not taken by the service provider)

GOODS TRANSPORT AGENCY (Sr. No.4 of 30/2012-ST)

- **Exemptions under the Mega Exemption Notification (ME-21)**
 - a) Services provided by a goods transport agency by way of transport of agricultural produce,[milk, salt, food grain including flours, pulses and rice], chemical fertilizers, organic manure, oilcakes, newspaper, magazines, relief materials, defence or military equipments, and cotton (ginned or baled)
 - b) Freight of Rs 750 for all goods transported for a single consignee/ Rs 1500 for a single carriage.

SPONSORSHIP SERVICE (Sr.No. 5 of 30/2012-ST)

- Services provided or agreed to be provided by way of **sponsorship** to any **'body corporate'** or **'partnership firm'** located in the taxable territory.
- **Definition under the Service Tax Rules, 1994**
 - Rule 2(bc) : body corporate has the meaning assigned to it in clause (7) of section 2 of the Companies Act, 1956*
 - Rule 2(cd): partnership firm includes a limited liability partnership*
- **Clause 7 of section 2 of the Companies Act, 1956**
 - body corporate" or" corporation' includes a company incorporated outside India but does not include-*
 - (a) a corporation sole;*
 - (b) a co- operative society registered under any law relating to co- operative societies; and*
 - (c) any other body corporate (not being a company as defined in this Act) which the Central Government may, by notification in the Official Gazette, specify in this behalf;*

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LEGAL SERVICES (Sr.No.6 of 30/2012-ST)

- **Legal services** provided by an arbitral tribunal or an individual advocate or firm of advocates to a **business entity** located in the taxable territory (Sr.No.6 of 30/2012)
- **Definition under the Service Tax Rules, 1994**
Rule 2(cca): *legal service means any service provided in relation to **advice, consultancy or assistance in any branch of law**, in any manner and includes representational services before any court, tribunal or authority.*
- **Definition of Business Entity**
Section 65B(17): *business entity means any person ordinarily carrying out any activity relating to industry, commerce or any other business or profession.*

LEGAL SERVICES (Sr.No.6 of 30/2012-ST)

- **Issues**

Whether services provided by advocates related to income tax, VAT, labour laws etc. liable under reverse charge?

- **Mega Exemption Notification (ME-6)**

a) Business entity with a turnover upto Rs 10Lakh

b) Services provided to other Advocates/Firm of Advocates

c) Non-business entities

* **SUPPORT SERVICES BY GOVERNMENT OR LOCAL AUTHORITY** (Sr.No. 7 of 30/2012-ST)

- Services provided by Government or local Authority to a **business entity** located in a taxable territory.
- **Government** defined w.e.f. 14/05/2015 under **section 65B(26A) of the Act** as
“Government means the Departments of the Central Government, a State Government and its Departments and a Union territory and its Departments, but shall not include any entity, whether created by a statute or otherwise, the accounts of which are not required to be kept in accordance with article 150 of the Constitution or the rules made thereunder”
- **Local Authority** also defined under **section 65(31) of the Act** to include a Panchayat, a Municipality, Municipal Committee, District Board, Cantonment Board, Regional Council, Development Board.
- * **The term ‘support services’ is replaced to ‘any service’ by the Finance Act,2015 with effect from a date yet to be notified.**

SUPPORT SERVICES BY GOVERNMENT OR LOCAL AUTHORITY (Sr.No. 7 of 30/2012-ST)

- **Issues**

- a) Whether statutory functions discharged by the government are covered under reverse charge?
- b) Whether Police Security provided to Actors covered under reverse charge?

- **Excludes (Government or Local Authority liable to discharge the liability)**

- a) Renting of Immovable Property Service
- b) Exclusions under the Negative List (Section 66D-Clause (a))
 - (i) Department of Posts by way of speed posts, express parcel post, life insurance and agency services provided to a person other than Government.
 - (ii) Services in relation to aircraft or vessel inside or outside the precincts of port or airport.
 - (iii) Transport of goods or passengers

DIRECTOR SERVICES (Sr.No. 8 of 30/2012-ST)

- Services provided by a director of a company or a body corporate to the company or body corporate. The Company or Body Corporate liable to discharge service tax under reverse charge.
- The term 'Body Corporate' has the meaning assigned to it in clause (7) of section 2 of the Companies Act,1956;
- **Issues**
 - a) Whether remuneration to executive/managing director of a company liable under reverse charge?
 - b) Whether payments made to directors in their professional capacity is liable under reverse charge?
 - c) Whether fees paid to directors of statutory bodies like RBI liable under reverse charge?

SERVICES PROVIDED BY MUTUAL FUND AGENTS AND DISTRIBUTORS (Sr.No.9 of 30/2012-ST)

- Services provided by Mutual Fund Agent or Distributor to a Mutual Fund or Asset Management Company .
- Earlier exempted vide clause 29(b) & (c) of the Mega Exemption Notification-25/2012.
- Exemption withdrawn w.e.f. 01/04/2015 and the Mutual Fund or Asset Management Company is liable under reverse charge.

SERVICES PROVIDED BY SELLING OR MARKETING AGENT OF LOTTERY TICKETS

(Sr.No10 of 30/2012-ST)

- Services provided by selling or a marketing agent of lottery tickets to a lottery distributor or selling agent, lottery distributor or selling agent liable under reverse charge.
- Negative List entry (i) in respect of betting, gambling or lottery deleted.
- Whether the Central Government is trying to trench on a subject of State Legislation?

Future Gaming Solutions Pvt. Ltd 2015(37) STR 65 (Sikkim).

“it is the exclusive legislative domain of the State legislature to levy tax of any nature on lotteries by virtue of entry 62 of List II to the Seventh Schedule”.

RENTING OF MOTOR VEHICLE SERVICE (Sr.No.11 of 30/2012-ST)

- Renting of a **Motor Vehicle** designed to carry passengers to a person not engaged in **similar line of business**.
- Reverse charge applicable in case of services received by **business entity registered as a body corporate** in a taxable territory from an individual /HUF/Partnership Firm/AOP in a taxable territory.
- **Motor Vehicle - Section 2(28) of the Motor Vehicle Act, 1988**, *“any mechanically propelled vehicle adapted for use upon roads whether the power propulsion is transmitted thereto from an external or internal source and includes a chassis to which a body has not been attached and a trailer; but does not include a vehicle running upon fixed rails or a vehicle of a special type adapted for use only in a factory or in any other enclosed premises or a vehicle having less than four wheels fitted with engine capacity of not exceeding thirty-five cubic centimetres;*
- Whether renting of buses is liable under reverse charge?

RENTING OF MOTOR VEHICLE SERVICE (Sr.No.11 of 30/2012-ST)

- Percentage of taxable value for the Service Receiver

Method followed by the service provider	Service Provider	Service Receiver
Avails the abatement (As per Sr. No. 9 and 9A of the abatement notification 26/2012-ST)		100% (100%*40%*14%)
Non-Abated Value	50%	50%

- Renting of Motor Vehicle which is not capital goods specifically excluded from the term 'input service'.
- Negative List – Entry O**
Metered Cabs or Auto Rickshaws

SUPPLY OF MANPOWER AND SECURITY SERVICES

(Sr.No.12 of 30/2012-ST)

- Reverse charge applicable in case of services received by **business entity registered as a body corporate** in a taxable territory from an individual /HUF/Partnership Firm/AOP in a taxable territory. 100% of service tax payable by the service receiver w.e.f. 01/04/2015
- **Definition provided under the Service Tax Rules,1994**
*Rule 2(g): “supply of manpower means supply of manpower, temporarily or otherwise, to another person **to work under his superintendence or control.***
- **[2015-TIOL-1602-CESTAT-MUM] Commissioner of Central Excise, Nagpur Vs. M/s Shri K M Sharma**
Charges levied on the basis of activities and material involved and not on the basis of number/nature or scope of manpower cannot fall under the category of ‘Manpower Supply and Recruitment Services’

WORKS CONTRACT SERVICES (Sr.No.13 of 30/2012-ST)

- Partial Reverse charge applicable in case of services received by **business entity registered as a body corporate** in a taxable territory from an individual /HUF/Partnership Firm/AOP in a taxable territory. Ratio of tax to be borne by -Service Provider: Service Receiver-50:50.
- Section 65B(54) of the Act defines the term Works Contract as
*“(54) "works contract" means a contract wherein **transfer of property in goods** involved in the execution of 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, improvement, repair, renovation, alteration of any building or structure on land or for carrying out any other similar activity or a part thereof in relation to any building or structure on land;*

WORKS CONTRACT SERVICES (Sr.No.13 of 30/2012-ST)

- **Service Tax Determination of Value Rules,2006**
- **Rule 2A(i):** The value of the service portion will be determined by deducting the value of property in goods transferred in the execution of works contract from the gross amount charged.
- **Rule 2A(ii)-**Where value has not been determined under clause(i), the value will be determined in the following manner.
 - a) Original Works: Taxable portion - 40%
 - b) Other than Original Works: Taxable portion - 70%

Original Work means new constructions, additions and alterations to abandoned or damaged structures,erection,commissioning or installation of plant,machinery or equipment.
- Whether service provider and receiver can adopt independent valuation methods?

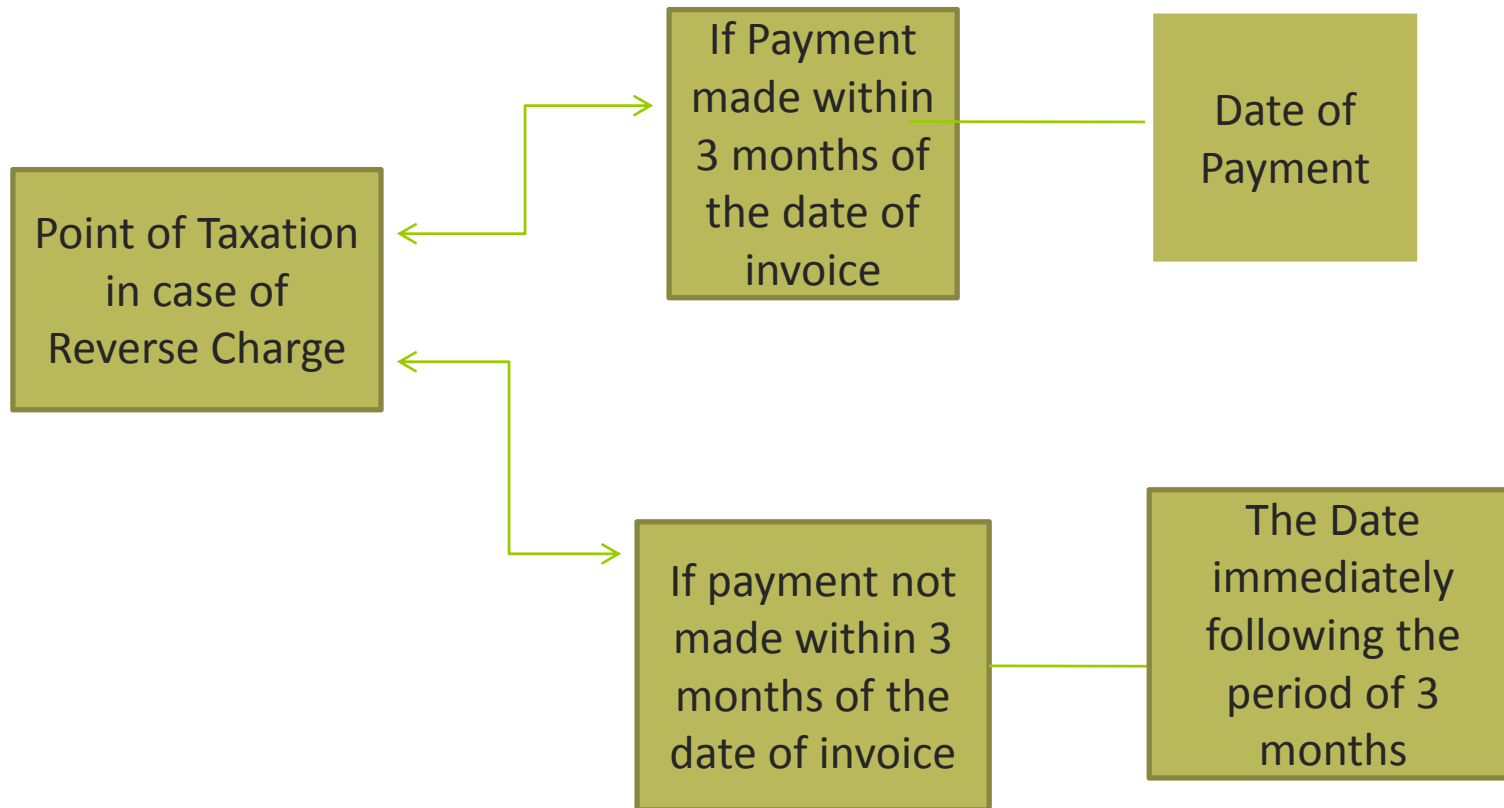
IMPORT OF SERVICES (Sr.No. 14 of 30/2012-ST)

- Taxable service provided or agreed to be provided by any person which is located in a **non-taxable territory** and **received** by any person located in the **taxable territory**.
- Whether the services are **received in India** was determined by the Taxation of Services (Provided from Outside India and Received in India) Rules,2006, which has been replaced by the Place of Provision of Services Rules,2012.
- **Mega Exemption Notification (ME-Entry 34)**
 - a) Services received from a non-taxable territory by Government, Local Authority, Governmental Authority or individual for purposes other than commerce, industry or any other business or profession,
 - b) Entity registered under section 12AA of the Income Tax Act,1961 for providing charitable activities,
 - c) a person located in a non-taxable territory.

POINT OF TAXATION RULES,2011

- ***Section 66B of the Act (charging section):** There shall be levied a tax at the rate of (fourteen) percent on the value of all services, other than those services specified in the negative list ,**provided or agreed to be provided** in the taxable territory by one person to another and collected in such a manner as may be prescribed.*
- These rules determine when the services are provided or agreed provided.
- Provisions to determine point of taxation w.r.t.:
 - Services generally provided;
 - Continuous supply of services;
 - Services to associated entities ;
 - Services liable under reverse charge
 - Change in effective rate of tax
 - Levy of tax on new services and special services.

REVERSE CHARGE MECHANISM (RULE-7)



GENERAL RULE (RULE-3)

- Point of taxation in case of a service provided in taxable territory shall be the earliest of following:
 - When a service is provided or agreed to be provided;
 - Issue of invoice; or
 - Receipt of payment/advance.
- In case invoice is not issued within time limit of 30 days from the **completion of taxable service**, point of taxation shall be the date of completion of provision of the service.
- **Circular No 144/13/2011-ST:** 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. Such auxiliary activities could include activities like measurement, quality testing etc. which may be essential pre-requisites for identification of completion of service.

GENERAL RULE (RULE-3)-CONTINUOUS SUPPLY OF SERVICE

- What shall constitute continuous supply:
 - ✓ Service provided or to be provided under a contract; and
 - ✓ Service to be provided continuously or on recurrent basis; and
 - ✓ The contract is for a period exceeding three months with the obligation of payment periodically or time to time; or
 - ✓ Central government can notify certain services to be in the nature of continuous supply
- Point of taxation in case of continuous supply shall be earlier of :
 - ✓ Invoice [to be issued within 30 days of completion of service]
 - ✓ Payment received
- Date of completion of service : each event which requires the service receiver to make any payment

ASSOCIATED ENTERPRISES

Associated Enterprises

Point of taxation in case of transactions with associated enterprises located outside India shall be earliest of the following:

- Date of payment;
- Date of debit in the books of accounts of the person receiving service

CHANGE IN THE EFFECTIVE RATE OF TAX

- In case of **change in effective rate of tax**, the point of taxation will be determined in the following manner: (change in rate effective from 01/06/2015)

Sr.No	Service Provided	Invoice w.r.t. rate change	Payment w.r.t change	Rate of Service Tax
1	Before Rate Change	After	After	14%
2	-do-	Before	After	12.36%
3	-do-	After	Before	12.36%
4	After rate change	Before	After	14%
5	-do-	Before	Before	12.36%
6	-do-	After	Before	14%

- Change in effective rate of tax will include a change in the portion of the value on which tax is payable.

NEW SERVICES & SPECIAL SERVICES

In case of **new services** taxed for the first time

- No tax will be payable to the extent invoice has been issued and payment received before such services became taxable;
- No tax will be payable if the payment is received before the services become taxable and the invoice is issued within fourteen days of the date when the service is taxed for the first time.

Special Services - Applicable in case of royalty payments for copyrights, trademarks, designs or patents.

In case consideration is not ascertainable at the time of performance of service, point of taxation shall be earliest of the following:

- Payment;
- Receipt of benefit by provider;
- Issue of invoice



THANK YOU

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