
**ANALYSIS OF PLACE OF PROVISION OF SERVICES RULES
&
TAXABLE PERSON AND REVERSE CHARGE MECHANISM**

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SYNOPSIS**

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PLACE OF PROVISION OF SERVICES

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1. Introduction to the situs of taxation and the new Charging Section

1.1 The Finance Bill, 2012 (“Bill”), rightly in the words of the Joint Secretary (Tax Research Unit), proposes to make a *‘paradigm shift in the way services are proposed to be taxed in future’* [a most notable feature in this budget]. A significant change is replacement of the existing charging section 66 by a new charging section 66B w.e.f. 1.7.2012. The new charging section 66B provides that there shall be levied a tax @12% of *‘the value of all services other than those specified in the negative list provided or agreed to be provided in the taxable territory, by one person to another...’*. Thus, section 66B clearly provides that the taxable event i.e. the ‘service’ must happen in the ‘taxable territory’. The term ‘taxable territory’ has been defined in the proposed section 65B(52) as *‘the territory to which the provisions of this Chapter apply’*. By section 64(1) Chapter V of the Finance Act, 1994 (i.e. the law governing service tax) extends to the whole of **‘India’** except the State of Jammu & Kashmir. The term ‘India’ has been defined in section 65B(27) which is given in **Annexure 1** attached and on reading of which it can be inferred that, broadly speaking taxable territory means India *minus* Jammu & Kashmir.

1.2 The Central Government has been empowered u/s. 66C to enact rules to determine when would the service be considered as provided in the taxable territory i.e. *rules to determine the place of provision of service*. The Place of Provision of Services Rules, 2012 [“PoP Rules”] is notified vide notification no. 28/2012-ST dated 20.6.2012 which is effective from 1.7.2012. These rules are analysed in paras below. CBEC have issued Taxation of Services – An Education Guide dated 20.6.2012, giving

detailed explanation on these rules in Guidance Paper 5 - “Place of Provision of Service Rules, 2012”. The analysis below is of the PoP Rules based on the said Education Guide. *Further, the PoP Rules would be effective for the first time in India. Hence we do not have any precedents.*

2. Place of Provision of Service Rules – General

Preliminary

- 2.1 The Place of Provision of Service Rules [“PoP Rules”] provide where a service is deemed to have been *provided*. *If the place of provision of service is* in the taxable territory it will be liable for service tax. If the place of provision of service is not within the taxable territory it will not be liable for service tax. The essence of the PoP Rules is that service is to be taxed in the jurisdiction of the place of consumption of service. In practice, the “*place of consumption*” i.e. the place where a service is used may not often be very easy to ascertain and may often lead to controversies. Hence the PoP Rules have been formulated specifically fixing the place of consumption by legislation. As the Education Guide clarifies ‘*nearest ‘proxies’ are adopted to provide specificity in the interpretation as well as application of the law.*’ The basic rule is that *the place of provision of service shall be the location of the service receiver. However, exceptions have been provided in case of performance based services, immovable property based services, certain specified services and transportation service etc. where other criteria such as location of service provider, location of performance of service, etc. are relevant. The location of service provider and location of service recipient is sought to be defined separately – write up of which is given in Annexure 2 attached.*

2.2 With the introduction of Place of Provision of Service Rules, the import and export rules¹ have been rescinded. The only requirement would be whether a service is provided in the taxable territory (pursuant to place of provision of service rules). If yes – liable, if no – not liable.

Purpose

2.3 The PoP Rules are intended to be relevant for the following:

- (i) Taxation of cross-border transactions in services.
- (ii) Transactions with service providers and service recipients in the state of Jammu & Kashmir and the rest of India. If service is provided in Jammu & Kashmir – not liable, if provided in rest of India – liable.
- (iii) Service providers operating within India with multiple locations and without centralized registration – the PoP Rules would be relevant in determining the jurisdiction applicable for their operations.
- (iv) Determination as to when a service is ‘wholly consumed’ in a Special Economic Zone (“SEZ”) to avail outright exemption.

3. Place of Provision of Service Rules – specific rules

General Rule – location of service recipient [rule 3]

3.1 The general or default rule is that the place of provision of a service shall be the *location of the service receiver* unless the transaction of service falls within any of the other rules mentioned below [paras 3.2 – 3.19]. The Education Guide sums up the impact of this rule as under:

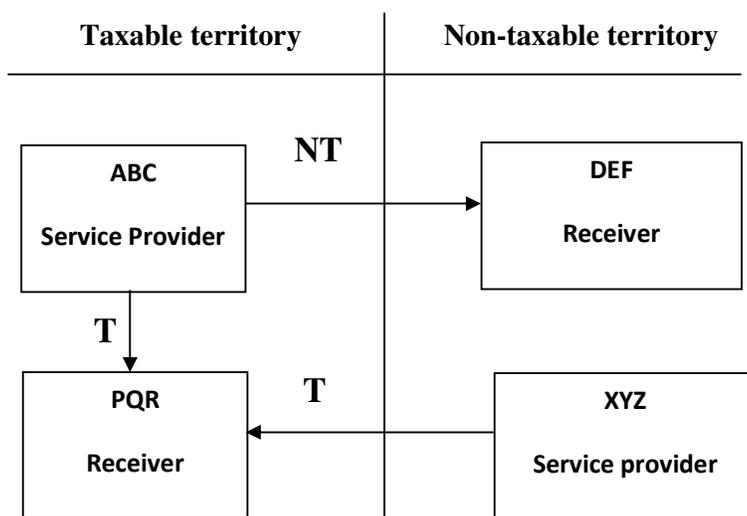
¹ The Export of Services Rules, 2005 and the Taxation of Services (Provided from Outside India and Received in India) Rules, 2006.

“The principal effect of the Main Rule is that:-

A. Where the location of receiver of a service is in the taxable territory, such service will be deemed to be provided in the taxable territory and service tax will be payable.

B. However if the receiver is located outside the taxable territory, no service tax will be payable on the said service.”

The above has been pictorially captured by the Education Guide as under:



T = Taxable NT = Non-Taxable

- 3.2 In case the location of the service receiver is not available in the ordinary course of business, the place of provision shall be the location of the service provider.

Place of provision of ‘performance based’ services to be location where the services are actually performed [rule 4]

- 3.3 The place of provision of ‘performance based services’ shall be the location where the services are actually performed. ‘Performance based’ services are categorized by the PoP Rules to be of 2 types viz.,:

- (a) services provided in respect of ‘goods’ that are required to be made physically available by the recipient of service to the provider of service, or to a person acting on behalf of the provider of service, in order to provide the service. E.g. repairs, courier, cargo handling, storage, technical testing, inspection, etc. The Education Guide has clarified that this category will not cover ‘goods’ provided by the service recipient which are only incidental to the provision of the service by the service provider e.g. free samples provided by a client – manufacturer to a market research agency to be distributed in order to conduct a survey. The above rule has two exceptions
- (i) when such services are provided from a remote location by way of electronic means the place of provision shall be the location where goods are situated at the time of provision of service. E.g. where a service provider does changes (like debugging) in the client’s software by accessing the client’s server through internet.
 - (ii) the performance based criteria will not apply in the case of a service provided in respect of goods that are temporarily imported into India for repairs, reconditioning or reengineering for re-export, subject to conditions as may be specified in this regard. No such conditions have been specified so far.
- (b) services provided to an individual, represented either as the recipient of service or a person acting on behalf of the recipient, which require the physical presence of the receiver or the person acting on behalf of the receiver, with the provider for the provision of the service. These are essentially personalized services e.g. beauty treatment, cosmetic surgery, classroom teaching, etc.

Place of provision of services relating to immovable property would be the location of immovable property [rule 5].-

3.4 The place of provision of the following services shall be the *place where the immovable property is located* or intended to be located [i.e. property to come into existence] :

- (i) services provided *directly in relation to* an immovable property e.g. construction, repair, renovation of a building or a civil engineering work; survey / exploration / exploitation of land and sea-bed, property management, etc. This would include services ‘upon’ or for bringing into existence an immovable property or services that alter the nature and value of the property or services for transfer of, or determination of title to, the property. This would not include services that have only an indirect bearing on an immovable property e.g., services of a tax consultant on capital gains on land or feasibility studies for a investment in a property, advice on property prices, etc.;
- (ii) services provided by experts and estate agents in relation to immovable property e.g. auctioneers, engineers, valuers, surveyors, **legal services** in relation to planning permission, etc.;
- (iii) provision of hotel accommodation by a hotel, inn, guest house, club or campsite, by whatever name called;
- (iv) grant of rights to use immovable property e.g. renting,
- (v) services for carrying out or co-ordination of construction work, including architects or interior decorators.

Place of provision of services relating to events to be the place where the event is actually held [rule 6]

3.5 The place of provision of the following services shall be the *place where the event is actually held*—

- (i) Services provided by way of –
 - (a) admission to; or
 - (b) organization of, and
- (ii) services ancillary to admission of a cultural, artistic, sporting, scientific, educational, or entertainment event, or a celebration, conference, fair, exhibition, or similar events. However, it is to be noted that admission to entertainment events and amusement facilities is covered in the Negative List [s. 66D(j)] and “entertainment event” has been defined in section 65B(24) to include concerts, drama, sporting events, etc. Hence admission to such entertainment events would not be liable for service tax and hence the PoP Rules would not be relevant for these events.

Place of provision of ‘performance based’ or ‘immovable property based’ or ‘event based’ services where they are provided at more than one location [rule 7].

- 3.6 Where any ‘performance based’ or ‘immovable property based’ or ‘event based’ services referred to paras 3.3 to 3.5 above are provided at more than one location, including a location in the taxable territory, its place of provision shall be the *location in the taxable territory where the greatest proportion of the service is provided*. E.g. where a firm provides technical inspection and certification services of a product to its client at Maharashtra (say, 20%), Kerala (say, 25%) and Colombo (say, 55%), then notwithstanding that the greatest proportion of the service is done at Colombo – a non-taxable territory, the place of provision of the entire service would be the place where the greatest proportion of the service within the taxable territory is done i.e. Kerala. Thus, in service exports even if a small percentage of the work is carried out in India, the exporter would lose export exemption. Similarly, in case of service imports, the

recipient maybe liable to pay service tax under reverse charge on the whole even if a small percentage of the work is carried out in India. Hence, the said rule would cause undue hardships in cases where the service providers are required to perform substantial part of their service outside the taxable territory and only a small part of the service is performed in India.

- 3.7 Under the present Export of Service Rules, 2005, if a 'performance based' service is partly performed outside India it would be considered as performed outside India and be entitled to export exemption. Under the PoP Rules, this exemption would not be available by virtue of the above rule. However similar imports would continue to be liable for service tax on the entire amount.

Where provider and receiver are located in taxable territory the place of provision of services shall be the location of service recipient [rule 8].

- 3.8 The basic philosophy of the PoP Rules is to fix the location where service is provided based on the consumption. The general rule (Rule 3) is that the place of provision of a service shall be the location of the service receiver unless the transaction of service falls within any of the other rules. In some cases, (as explained above) the place of provision of service is based on the other criteria viz., where -

- (i) the service is actually performed (Rule 4); or
- (ii) the land is located (Rule 5); or
- (iii) the event is actually held (Rule 6).

However, Rule 8 of the PoP Rules overrides rule 4, 5 and 6 by providing that where the location of the service provider as well as that of the service receiver is in the taxable territory, the place of provision of the service shall be the location of the service receiver. The implication of

this rule is that it overrides rules 4 to 6 (paras 3.3 to 3.5). For e.g. the place of provision of helicopter repair services performed in Nepal would be Nepal (i.e. non-taxable territory) by virtue of rule 4(a) [refer para 3.3]. But if the service provider and the service receiver are located in India (e.g. Hindustan Aeronautics Ltd. – the service provider and Pawan Hans Ltd. – the service recipient) the services would be considered as provided in India (in the taxable territory), notwithstanding rule 4.

- 3.9 In this regard the following maybe noted. It appears that rule 4, 5 and 6 is necessary since the nature of services envisaged in the said rules indicate that the services are consumed where -
- a. it is actually performed (Rule 4); or
 - b. the land is located (Rule 5); or
 - c. the event is actually held (Rule 6).

Thus it is dependent on where the services have been utilized and not where the provider or receiver of service is located. If the services covered in rule 4, 5 and 6 of the PoP Rules are utilized outside the taxable territory the consumption of the services can be said to have taken place outside the taxable territory. The mere fact that both the service provider and service receiver are located within the taxable territory may not alter the above position. However, the philosophy of the PoP rules is otherwise. The intention of rule 8 it appears is to trigger the ‘proxy’ rule and consider the location of service recipient as place of provision and not where the service is actually utilized in a case where the service provider and recipient are based in the taxable territory!

- 3.10 However, even if the place of provision of service is in the taxable territory but the provider and the receiver of the service are located outside the taxable territory, the services are exempted vide entry 34(c) of

Notification no. 25/2012-ST dated 20.6.2012. Thus, if a French architect provides a UK company certain designs for an office to be located in India the place of provision of the services by virtue of rule 5 would be in the Taxable Territory. However, it would be exempt from service tax due to Notification no. 25/2012-ST dated 20.6.2012.

Place of provision of ‘specified services’ shall be the place of service provider [rule 9].

3.11 The place of provision of the following ‘specified services’ shall be the *location of the service provider*:

- (a) Services provided by a banking company, or a financial institution, or a non-banking financial company, to ‘account holders’. The Education Guide clarifies that the place of provision of services normally provided to account holders in the ordinary course of business e.g. operation of bank accounts, transfer of money, lending etc. would be the location of service provider. But services not provided to account holders in the ordinary course of business e.g. financial leasing, merchant banking, securities and forex broking, advisory services, etc. would be the location of service recipient (rule 3 – para 3.1 above – default rule);
- (b) Online information and database access or retrieval services;
- (c) Intermediary services (see para 3.12 below);
- (d) Service consisting of hiring of means of transport, upto a period of one month.

3.12 An ‘intermediary’ is defined in rule 2(f) as meaning “*a broker, an agent or any other person, by whatever name called, who arranges or facilitates a provision of **service** (hereinafter called the main service) between two or more persons, but does not include a person who*

provides the main service on his account.” The Education Guide has clarified the following points -

- (a) There are two supplies in a situation involving an intermediary-
 - (i) the supply of services by the principal to a third party;
 - (ii) the supply of services by the intermediary to the principal.An intermediary is essentially an agent, whose services to his principal are clearly identifiable and have a distinct value and who cannot alter the nature and value of the supply made by the principal to the third party.
- (b) An intermediary for goods (e.g. a commission agent for goods or a stock broker) is not covered by this rule but only an intermediary for services is covered. The place of provision of the services of an intermediary for goods is the location of service recipient.
- (c) A person who arranges or facilitates the provision of service (referred to as main service) but provides the main service on his own account is also not covered by this rule.

Further, the Education Guide gives the following examples of intermediaries:

- (i) Travel Agent (any mode of travel);
- (ii) Tour operator
- (iii) Commission agent (for services)
- (iv) Recovery agent.

3.13 A freight forwarder who buys-in and sells freight transport as a principal would not be regarded as an intermediary and place of provision of service which in this case will be place of transportation of goods will be governed by rule 10 [refer para 3.14]. However, if the freight forwarder acts as an agent of an importer or an exporter by arranging freight transport, he would be considered as an ‘intermediary’ and place of

provision of service would be his location. The Education Guide has also clarified that the call centres who provide services to their clients by dealing with the customers of the clients on the client's behalf, but actually provide these services on their own account, will not be categorized as intermediaries.

Place of provision of goods transportation services other than a goods transportation agency services shall be the place of destination of goods [rule 10].

- 3.14 The place of provision of services of transportation of goods (except by a goods transportation agency or by way of mail or courier) shall be the *place of destination of the goods*. Thus, services provided by shipping lines / airlines for transportation of goods from India to a place outside India (exports) would not be liable (since it would be considered as provided in non-taxable territory). As regards imports i.e. services provided by shipping lines / airlines for transportation of goods from a place outside India to a place in India, the place of provision of service is India. However, it may be noted that the services by way of transportation of goods by an aircraft or vessel from a place outside India to the customs station of clearance in India is an item in the negative list [section 66D(p)] and hence would not be taxable.

Place of provision of services of a goods transportation agency (GTA) shall be the location of the 'person liable to pay tax' [rule 10 - proviso]

- 3.15 The place of provision of service in case of GTA services shall be *location of the person liable to pay tax*. In terms of rule 2(1)(d)(i)(B) of the Service Tax Rules, 1994, for services of goods transportation agency services in case of specified categories of consignors / consignees it

would be the person liable to pay the freight who is the person liable to pay service tax and if such person is located in non-taxable territory it is the GTA who would be made liable to pay service tax.

Place of provision of passenger transportation services shall be the place of embarkation for ‘continuous journey’ [rule 11]

- 3.16 The place of provision in respect of a passenger transportation service shall be the *place where the passenger embarks on the conveyance for a continuous journey*. Continuous journey means a journey for which –
- (a) a single ticket is issued; or
 - (b) more than one ticket or invoice is issued at the same time, either by one service provider or through one agent acting on behalf of more than one service provider,
- and which involves no stopover between any of the legs of the journey for which one or more separate tickets or invoices are issued.

Place of provision of services provided on board a conveyance [rule 12].

- 3.17 Place of provision of services provided on board a conveyance during the course of a passenger transport operation, including services intended to be wholly or substantially consumed while on board, shall be the *first scheduled point of departure of that conveyance* for the journey. The example given by Education Guide is as under:

“A video game or a movie-on-demand is provided as on-board entertainment during the Kolkata-Delhi leg of a Bangkok-Kolkata-Delhi flight. The place of provision of *this service will be Bangkok (outside taxable territory, hence not liable to tax).*”

If the above service is provided on a Delhi-Kolkata-Bangkok-Jakarta flight during the Bangkok-Jakarta leg, then the place of provision will be Delhi (in the taxable territory, hence liable to tax).”

Powers to notify description of services or circumstances for certain purposes [rule 13].

- 3.18 In order to prevent double taxation or non-taxation of the provision of a service, or for the uniform application of rules, the Central Government shall have the power to notify any description of service or circumstances in which the place of provision shall be the '*place of effective use and enjoyment of a service*'.

Tie breaker test – later rule to apply [rule 14]

- 3.19 Where the provision of a service is, *prima facie*, determinable in terms of more than one rule discussed above, it shall be determined in accordance with the ***rule that occurs later*** among the rules that merit equal consideration.

Summing up

- 3.20 The above rules maybe summed up in a table as under:

Sl. No.	Description of service	Place of Provision of service
1.	All services (except if specifically covered below)	Location of service recipient. If location of service recipient not available in ordinary course, location of service provider.
2.	Specified ' <i>performance based</i> ' services	Location of performance of service
3.	Services relating to ' <i>immoveable property</i> '	Where the immoveable property is located or intended to be located
4.	Services relating to ' <i>events</i> '	Where the event is actually held
5.	Performance based / immoveable property based / event based services provided at more than one location.	Location in the taxable territory where the greatest proportion of service is provided.
6.	Where the service provider and receiver are located in the taxable	Location of service recipient notwithstanding the location of

	territory	performance, immovable property or event
7.	Specified services	Location of service provider
8.	Goods transport (other than by a goods transportation agency or by way of mail or courier)	Location of destination of goods
9.	Goods Transport Agency services (i.e. transport by road in a goods carriage)	Location of the person liable to pay service tax.
10.	Passenger transportation services	Place of embarkation for 'continuous journey'
11.	Services on-board a conveyance	First scheduled point of departure
12.	Services <i>prima facie</i> fitting into two or more of the above rules - tie-breaker	Later rule to apply

4. **Other Provisions**

4.1 **Export of Services [Rule 6A of Service Tax Rules, 1994] :**

Export of services shall now be governed by new Rule 6A of the Service Tax Rules 1994. The essential requisites before a service can be designated as export service are:

- It must be a service as defined under sub-section 44 of section 65B;
- the service provider must be located in the taxable territory;
- the service receiver must be located outside India;
- the service is not a service specified in the negative list;
- the place of provision of the service is outside India;
- the payment for such service is received by the service provider in convertible foreign exchange; and
- the service provider and service receiver are not merely establishments of a distinct person under Explanation 2(b) [should read as Explanation 3(b)] of clause 44 of s. 65B(44) of the Act [see Annexure 2 – para 13].

All the above conditions must be satisfied to avail the status of export of service. If the service qualifies to be an export of service, service provider can avail Cenvat Credit of service tax paid on the input services used for export of services and rebate of the service tax paid on the said input services can be claimed under notification no. 39/2012-ST dated 20.6.2012.

4.2 ***Date of determination of rate of tax, value of taxable service and rate of exchange.*** A new section 67A has been inserted w.e.f 28.5.2012 to prescribe the relevant date for the application of rate of exchange, valuation or rate of service tax. The new section provides that the rate of service tax, value of a taxable service and rate of exchange, if any, shall be the rate of service tax or value of a taxable service or rate of exchange, as the case may be, in force or as applicable at the time when the taxable service has been provided or agreed to be provided. The time when the taxable service has been provided or agreed to be provided is determined under the Point of Taxation Rules, 2011. This section would address the issue with regard to the rate of exchange that must be applied to determine the value of a taxable service where invoiced amount is in foreign currency. In such cases, the rate of exchange applicable shall be the rate prevailing at the time when services are deemed to have been provided as per the PoT Rules i.e. date of issue of invoice/date of payment/date of completion of service as the case may be. The rate of exchange would be the Customs notified exchange rates under the *Explanation* to section 14 of the Customs Act, 1962.

5. Taxable Person and the Reverse Charge Mechanism

5.1 Section 68 of the Act read with rule 2(1)(d)(iv) of the Service Tax Rules, 1994 together determine the 'taxable person' i.e. the 'person liable to pay service tax'. In all cases except in case of certain notified services, the service provider is liable to pay service tax. However, under section 68(2) the Central Government can notify –

- (a) the services where a person other than a service provider (e.g. the service recipient) can be made liable to pay service tax; and
- (b) the extent to which service tax would be payable by such person and the service provider.

The Central Government has issued notification no. 30/2012-ST dated 20.06.2012 which is effective from 1.7.2012 under section 68(2) of the Act.

5.2 The 'taxable person' and the extent to which tax would be payable by him is indicated in the table below.

Sl. No.	Description of Taxable Service	% of Service Tax Payable	
		Service Provider	Service Receiver
1.	Insurance agent's services to Insurers	Nil	100%
2.	Goods Transport Agency (GTA) services for specified consignors/consignees (See Note 1)	Nil	100%
3.	Sponsorship services to Corporates /Firms/LLPs located in the taxable territory	Nil	100%
4.	Advocate's/Legal firm's/Arbitral Tribunal's services to business entities located in taxable territory	Nil	100%
5.	Support services (except renting of immovable	Nil	100%

	property) by Government or local authority to business entities		
6.	Services provided to corporate business entities located in taxable territory by Individuals/HUF/ Firm/LLP/ AOP located in taxable territory (a) Motor Vehicle renting services to corporates not in similar line of business ➤ Abatement claimed ➤ Abatement not claimed (b) Supply of Manpower (c) Works Contract Services (See Note 2)	Nil 60% 25% 50%	100% 40% 75% 50%
7.	Services provided by any person located in non taxable territory and received by any person located in taxable territory	Nil	100%
8.	In all other cases	100%	Nil

Notes:

1. The person liable to pay the freight provided he is located in the taxable territory would be the service recipient in case of GTA services. If person liable to pay freight is located in the non-taxable territory, the GTA would be liable to pay the service tax.
2. In works contract services, where both service provider and service recipient is the person liable to pay tax, the service recipient has the option of choosing the valuation method as per choice, independent of valuation method adopted by the provider of service.
3. Reverse charge on services provided by mutual fund distributors to Mutual funds / asset management companies has been deleted post 1.7.2012 in view of exemption provided to the services of the Mutual Fund Agent / Mutual Fund Distributor.

Definition of 'India'

Section 65B(27)

India means-

- (i) The territory of the Union as per clauses (2) & (3) of article 1 of the Constitution i.e. the state territories and the union territories;
- (ii) The 'territorial waters', continental shelf, exclusive economic zones and other maritime zones as defined in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976 i.e. upto 200 nautical miles;
- (iii) The sea bed and sub-soil underlying the territorial waters [upto 12 nautical miles];
- (iv) The airspace above its territory and territorial waters [upto 12 nautical miles]; and
- (v) installations, structures and vessels located in the continental shelf and exclusive economic zone of India for the purposes of prospecting or extraction or production of mineral, oil and natural gas and supply thereof.

Location of service provider and service recipient

Rules to determine Location of service provider and service recipient

1. The ascertainment of location of the service provider and the service recipient are significant in the PoP Rules.

2. The “***location of the service provider***” is ascertained by the application of the following rules *in seriatum* -
Rule 1: where the service provider has obtained a single registration, whether centralized or otherwise, the premises for which such registration has been obtained.
Rule 2: where the service provider is not covered by rule 1 above, the location of service provider would be determined by the following rules applied in the following order:
 - (i) the location of his ‘*business establishment*’; or
 - (ii) where the services are provided from a place other than the business establishment, that is to say, a ‘*fixed establishment*’ elsewhere, the location of such establishment; or
 - (iii) where services are provided from more than one establishment, whether business or fixed, the *establishment most directly concerned* with the provision of the service; and
 - (iv) in the absence of such places, the *usual place of residence* of the service provider.

3. The “***location of the service recipient***” is ascertained by the application of the following rules *in seriatum* –

Rule 1: where the service receiver has obtained a single registration, whether centralized or otherwise, the premises for which such registration has been obtained;

Rule 2: where the service recipient is not covered by rule 1 above, the location of service recipient would be determined by the following rules applied in the following order:

- (i) the location of his *business establishment*; or
- (ii) where services are used at a place other than the business establishment, that is to say, a *fixed establishment* elsewhere, the location of such establishment; or
- (iii) where services are used at more than one establishment, whether business or fixed, the *establishment most directly concerned* with the use of the service; and
- (iv) in the absence of such places, the *usual place of residence* of the service receiver which in case of telecommunication service, shall be the billing address.

4. The terms ‘establishment’, ‘business establishment’, ‘fixed establishment’, ‘establishment most directly concerned in providing the service’, etc. have not been defined in the law. Hence meanings of these terms are to be ascertained as is generally understood and in the context in which they are used. As regards the term *usual place of residence*, it is defined only for body corporates as the place of incorporation or where they are legally constituted. The terms are explained below.

Establishment

5. The Black’s Law Dictionary - 6th edition – page 546 defines the term “establishment” as follows:

“**Establishment.** An institution or place of business, with its fixtures and organized staff. *Abnie v. Ford Motor Co.* Ohio Com. Pl. 195 N. E. 2d 131, 135. State of being established.”

Thus, the term establishment envisages a structure or a place as well as human resources to conduct the business. A ‘*branch*’ or ‘*agency*’ or ‘*representational office*’ in any territory is considered to be an ‘establishment’ in the territory [Explanation 3 to s. 65B(44)].

6. An establishment could be a ‘business establishment’ or a ‘fixed establishment’.

Business Establishment

7. The Education Guide clarifies that “*a business establishment is the place where the essential decisions concerning the general management of the business are adopted, and where the functions of its central administration are carried out. This could be the Head Office or a factory or a workshop or shop / retail outlet. Most significantly , there is only one business establishment that a service provider or receiver can have.*” In this context one may also usefully refer to the TRU circular dated 27.7.2005 which in the context of the erstwhile explanation to s. 65(105) had clarified as follows: “*The business establishment is the principal place of business, usually head office or headquarters or the seat from which business is run. There can be only one such place. A business may have headquarters in one country but branches in many other countries. A company may be incorporated in one country but does the business entirely from a head office in another country. In such cases, business establishment is treated to be in a country where the business is entirely done from the head office.*”

Fixed Establishment

8. The term “fixed establishment” consists of two words “fixed” and “establishment”. As explained in para 5 above an “establishment” is a place having a structure and human resources to carry on business. Further the word “fixed” would denote that the establishment must have a sufficient degree of permanence. Thus, the definition of the term as clarified in the Education Guide i.e. “*a place (other than a business establishment) which is characterized by a sufficient degree of permanence and suitable structure in terms of human and technical resources to provide the services that are to be supplied by it, or to enable it to receive and use the services supplied to it for its own needs.*” would be within the normal meaning of the term. In a nutshell three factors are determinative of a ‘fixed establishment’: (i) a **p**lace; (ii) **p**eople, (iii) with a degree of ‘**p**ermanence’ [the three PPPs like a three piece suit!].

Illustrations

(Per Education Guide –para 5.2.7 – illustrations 2 &3)

- An overseas business house sets up offices with staff in India to provide services to Indian customers. Its fixed establishment is in India.
- A company with a business establishment abroad buys a property in India which it leases to a tenant. The property by itself does not create a fixed establishment. If the company sets up an office in India to carry on its business by managing the property, this will create a fixed establishment in India.

Usual Place of Residence

9. The term ‘usual place of residence’ for a ‘body corporate’ (i.e. incorporated bodies) is defined by the *Explanation to* clauses (h) and (i) of rule 2 to mean the place of incorporation or where they are legally constituted. As regards individuals, to whom the criterion of ‘usual place

of residence’ would apply more appropriately the TRU circular clarifies the meaning of the term as follows:

“The usual place of residence of an individual is the place (country, state, etc.) where the individual spends most of his time for the period in question. It is likely to be the place where the **individual has set up his home, or where he lives with his family and is in full time employment.** Individuals are not treated as belonging in a country if they are short term, transitory visitors (for example if they are visiting as tourists, or receive medical treatment or for a short term language / other course). **An individual cannot have more than one place of usual residence.**”

Establishment most directly concerned in providing/ receiving a service relevant.

10. The rules provide that where services are provided / received from more than one establishment, whether business or fixed, the *establishment most directly concerned* with the provision / receipt of the service would be relevant. Thus, where a provider who has his headquarters in the US and a branch in India provides services directly from his headquarters to an Indian company, the location of the service provider would be US (i.e. outside the taxable territory) although he has an establishment in India and the location of service recipient would be India i.e. taxable territory. However, where the Indian branch provided services to the Indian company, the location of both the service provider and service recipient would be India.
11. In this context, in order to ascertain the ‘*establishment more directly concerned in providing the service*’, the Education Guide provides guidance as follows:

“This will depend on the facts and supporting documentation, specific to each case. The documentation will include the following:-

- the contract(s) between the service provider and receiver;
- where there are no written contracts, any written account (documents, e-mail etc) between parties which sets out in detail their understanding of the oral contract;
- in particular, for suppliers, from which establishment the services are actually provided;
- in particular, for receiver, at which establishment the services are actually consumed, effectively used or enjoyed;
- details of how the business fits into any larger corporate structure;
- the establishment whose staff is actually involved in the execution of the job;
- performance agreements (which may be indicative both of the substance and actual nature of work performed at a particular establishment).”

12. In this regard, the concept of ‘*establishment more directly concerned in providing the service*’ is to be tested in Indian Courts in the context of service tax. Here one judicial pronouncement in the context of UK VAT law maybe referred which has evolved a test. In *Chinese Channel (Hongkong) Ltd. v. Commissioners of Customs and Excise* (1998) Simon’s Tax Cases 347 (High Court of Justice – Queens Bench Division, UK), a Hongkong company (CCHK) provided broadcasting services to its subscribers in Europe (including UK). CCUK an associated company in the UK solicited subscriptions, checked credit ratings and collected the subscriptions. CCUK also engaged in editorial and production of the tapes it received from CCHK and also provided local community news services. On facts, the Court found that CCUK was a fixed establishment in the UK though a separate legal entity since it was not independent of CCHK. The issue then was whether the service is supplied from the fixed establishment. The Court held that in order to determine this: “*It is not just a matter of comparing the activities of the two companies. It is more important, ..., to consider the significance of those activities and the part*

they play in their contribution to the service supplied ...” The Court held that the services provided to the subscribers “*was the facility of receiving broadcasts selected by CCHK. This consisted of the provision of a right, the transmission of programmes and the content of those programmes.*” This the Court held was provided by CCHK from Hongkong and not by CCUK from UK. Thus, in order to ascertain the ‘*establishment more directly concerned in providing the service*’ the test adopted is to consider the significance of the activities performed by the establishments in question and the part they play in their contribution to the service supplied.

Establishment in taxable territory and non-taxable territories of a person are considered as separate entities

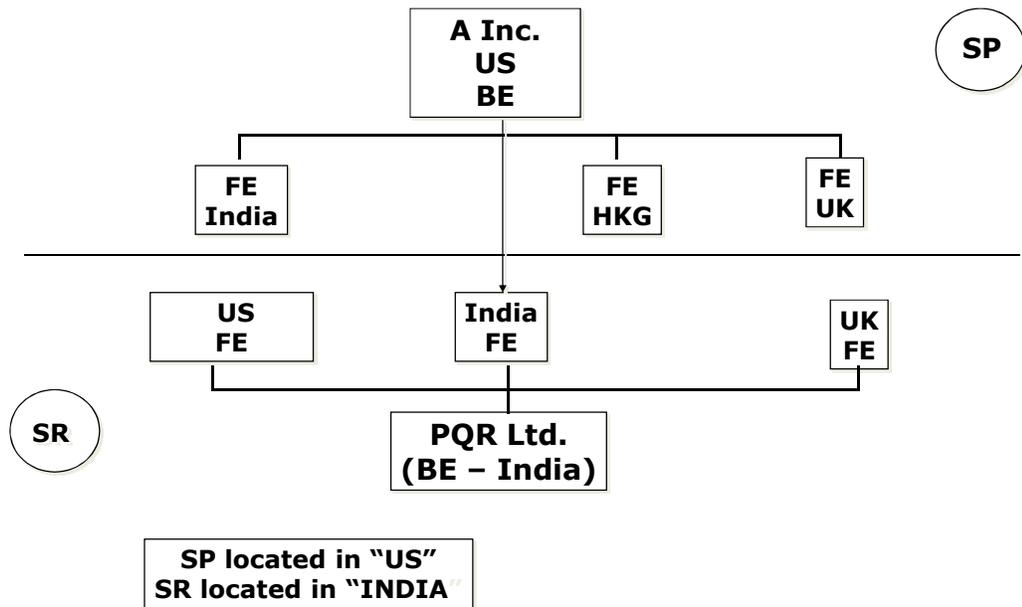
13. A ‘*branch*’ or ‘*agency*’ or ‘*representational office*’ in any territory is considered to be an ‘*establishment*’ in the territory [Explanation 3 to s. 65B(44)]. Further, Explanation 3(b) to s. 65B(44) defining the term ‘*service*’ provides that an establishment (e.g. branch, agency or representative office) of a person located in the taxable territory and another establishment of such person located in a non-taxable territory will be separate persons.
14. One consequence of the above would be that a transaction between say, a US Head office of a company and its Indian branch would be considered as ‘*service*’ with the location of the service provider as US (outside the taxable territory) and the location of the service recipient would be India (taxable territory).
15. Another consequence of the rule stated above is that where the service provider / recipient has a business / fixed establishment in several

countries each of these establishments would be treated as separate persons and accordingly, the location of the service provider / recipient vis-à-vis the particular service would be determined by this rule. For e.g. where the US branch of an Indian company receives services from its overseas suppliers the location of both the service provider and service recipient would be considered as outside the taxable territory.

Diagrammatic examples of application of the rules to determine location of Service Provider and service recipients

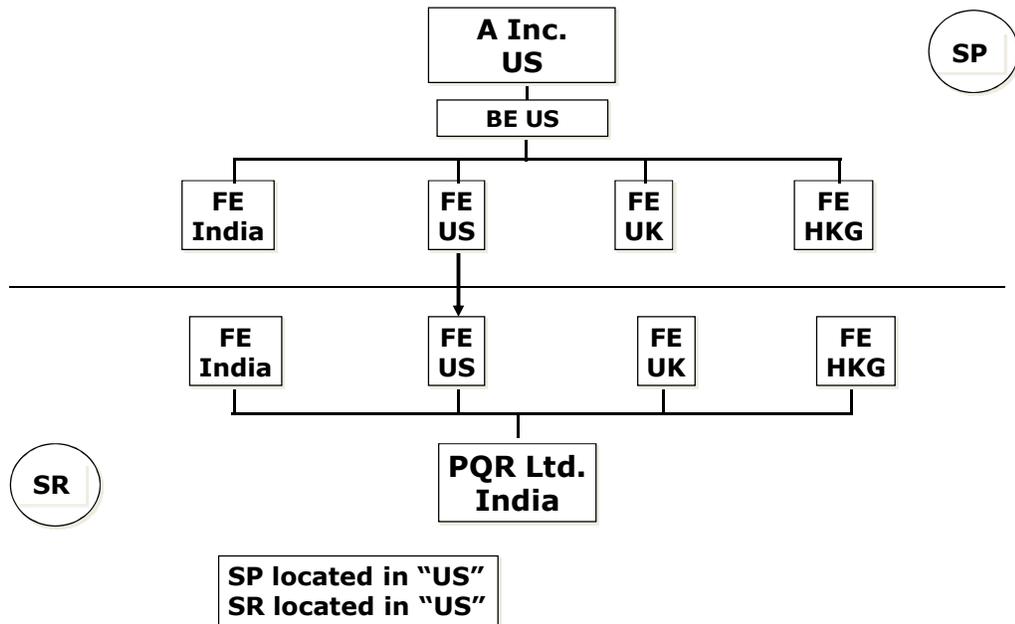
16. The application of the above rules to determine location of Service Provider (SP) and Service Recipient (SR) can be explained by way of diagrammatic examples.

Example 1



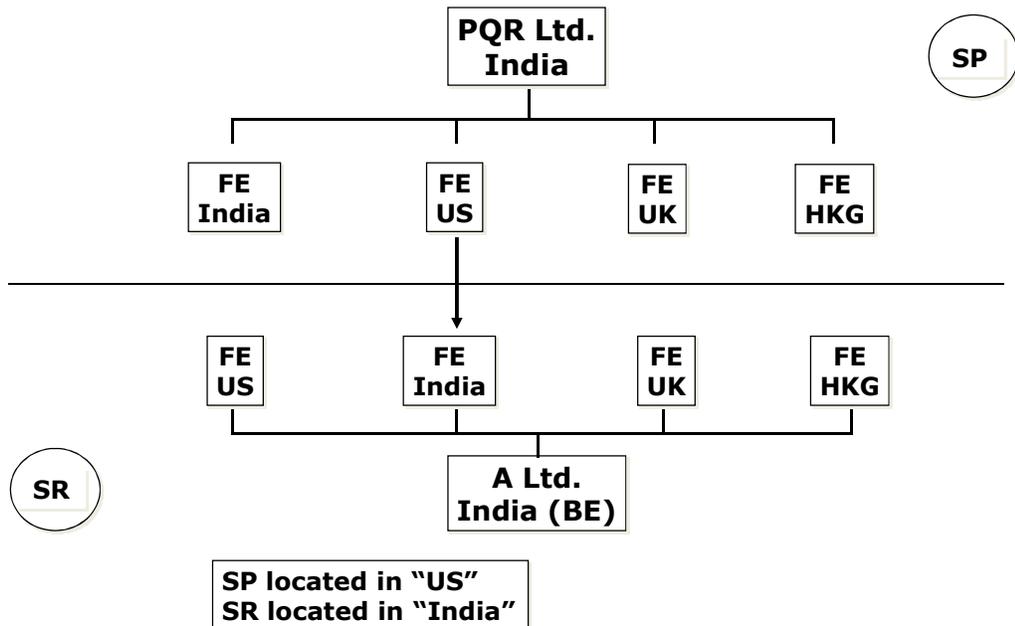
Business establishment of A Inc. a US company provides services directly to a fixed establishment of an Indian Company PQR Ltd.

Example 2



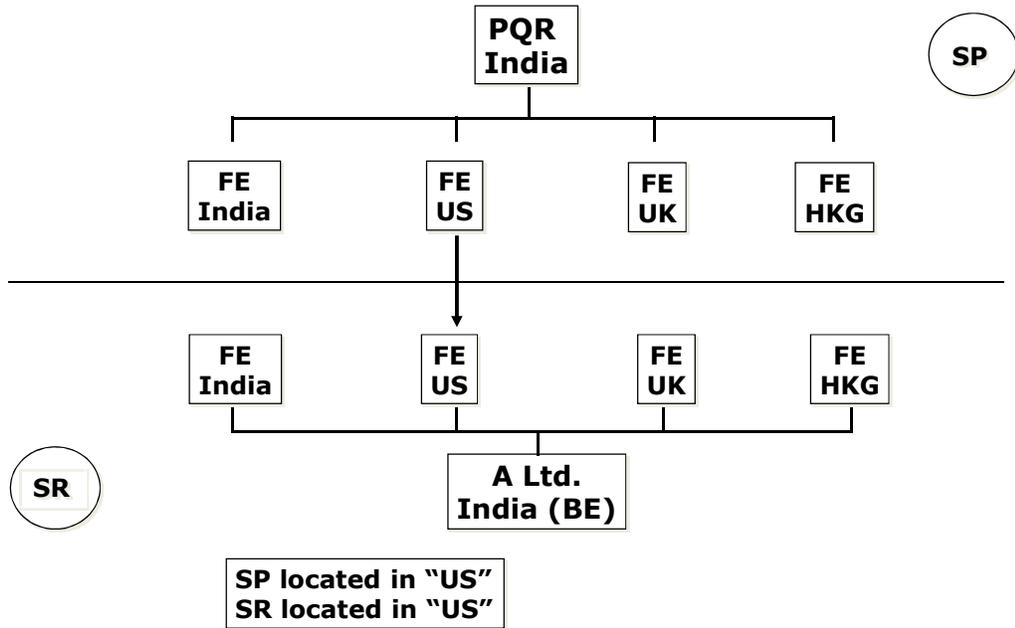
US Fixed establishment of A Inc. a US company provides services to a US Fixed establishment of an Indian Company PQR Ltd.

Example 3



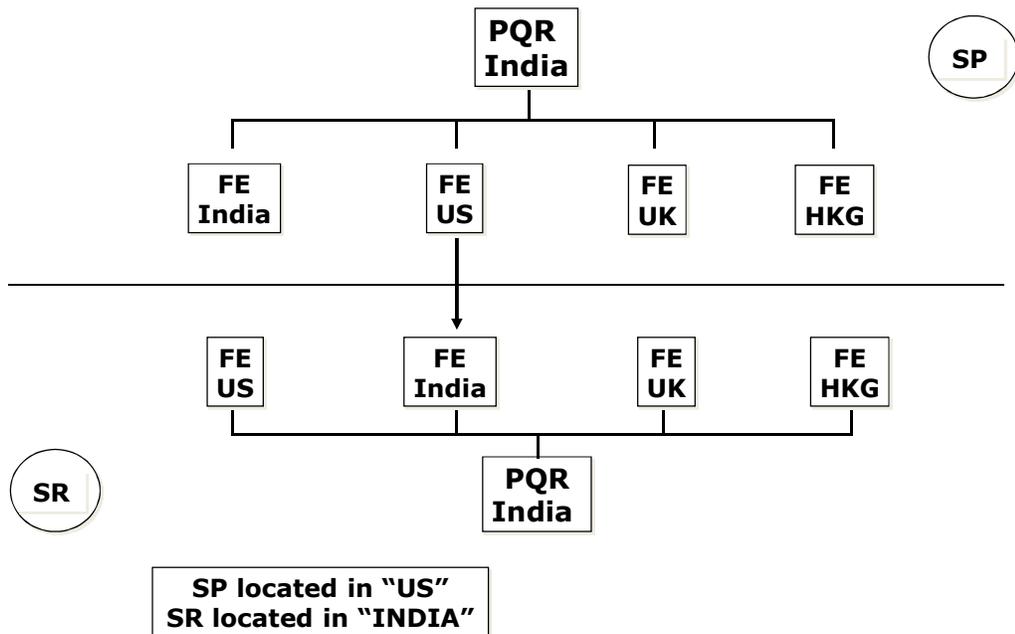
US Fixed establishment of PQR Ltd. an Indian company provides services to the Indian Fixed establishment of an Indian Company A Ltd.

Example 4



US Fixed establishment of PQR Ltd. an Indian company provides services to a US Fixed establishment of an Indian Company A Ltd.

Example 5



US Fixed establishment of PQR Ltd. an Indian company provides services to an Indian Fixed establishment of the **same** Indian Company PQR Ltd.