

## Technology Contract- VAT Vs ST

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This category covers information technology, IT enabled service and telecommunication industry. Today businesses are done in various complex manner through different jurisdictions in different countries.

They could be : Software and hardware supply, turnkey contracts, Build Operate Transfer, Build Own Operate and Transfer, software as a service, professional supply service are different modes of doing business. The dominant motive of the transaction, applicability of aspect theory, whether contracts are vivisectable, whether license transfer is involved goods or service being transferred], situs of sale and the mode of delivery are basic principles which should be known for understanding the transaction. The same are briefly discussed below:

- a. Dominant Motive – The intention of entering into a transaction is important and critical while arriving at the tax implication. Example – A technology company provides educational support for an international school. It may require to procure software like Learning management solutions and licenses to do so. It may also require to use servers for being able to provide the education online. However as the intention is to impart the services of education it would be under service tax and not liable to VAT. Recent SIM Card decision on Idea Cellular by SC observes that SIM card is part of the service and consequently no VAT should be chargeable.
- b. Aspect Theory – The Apex court has held that the same transaction is liable to be taxed on different aspects/ events. Example is manufacture of product to be sold suffers excise duty on manufacture and also VAT/ CST. SC in the case of Imagic Creative however has observed that where VAT is applicable service tax should not be levied. That they are mutually exclusive.
- c. Vivisectable Contracts – Lump sum contracts where bifurcation between different activities does not exist may not be artificially vivisectable. Courts have ruled that as far as works contracts or supply of food contracts are considered it is possible to do so as [Article 366\(29A\)](#) specifically provides for the same.
- d. Transfer of License – for goods or service? – This issue may require more judicial clarity as on date.
- e. Situs of sale – Under VAT one needs to follow the goods. However in case of intangible goods how can one do that? The location of the server, place of contract licensee, dealer of

software etc may also lead to some amount of uncertainty.

- f. Mode of delivery – When programs are on media and sold- shrink wrapped etc then there is no doubt that it is goods. However when the same is downloaded how we know from where it has started, where it is delivered.

Further the examination of the different common types of transactions may shed some light on the various tax alternative and the treatment.

1. Development of software and sale on media- This has been clearly held to be goods and even Customs duty are liable on the same. VAT liable.
2. Development of software and transmission by way of electronic download. The liability under service tax on the same has led to some amount of discontent and tax payers questioning as to under which tax it should be covered. However until centre & state do not resolve this issue the liability under VAT continues.
3. Sale of licenses: This is a deemed sale as it is right to use the software for a particular period and the software is goods. Liable for VAT.
4. Customised Software: When one sells customised software to the customer as per their needs it is a sale liable to VAT. It is also subjected to service tax.
5. Customisation on software owned by customer: This is akin to a job work on other material. The service of working on the program owned by the client where the property of the developed program does not accrue to the vendor but is always the property of the customer. No VAT liability.
6. Manpower supply services: Many BPO/ KPO companies hire out professionally qualified persons of certain competencies such as java + Linux – Level 2 and bill the customers on number of days. Here the customer directs the professionals to do his bidding as per his instructions. There is no transfer of goods and therefore VAT is not applicable.
7. Implementation of software / Calibration of software/ Going live: There is no transfer of property as one enables or disables the various masters, controls to make the software run as required by the customer. It is a pure service.
8. Disaster Management : This is a service which maybe taken up as a preventive measure or corrective after happening of the disaster. Wherever goods [ hardware / ready software] are transferred or right to use goods are provided it would be liable to VAT. Where the service provider provides the service of mirroring, alternative site with his own equipment like

servers, cloud etc, it would only be a service.

9. Updates and upgrades [ Patches]: These are smaller programs and therefore liable to VAT.
10. Testing: Confirming the functionality or usage of the software programs. Pure service no programs transferred. Only service tax leviable.
11. Debugging: Again a trouble shooting exercise akin to testing but goes beyond and corrects the same. Maybe like repairs. Only if any program transferred then there is a liability.
12. Maintenance of software: This maybe a works contract or a service contract. If works contract liable if service contract not liable.
13. Software as a service if on server / cloud: This is a new methodology where the control and possession of the data/ programs being accessed remain with the service provider [ ISP] which maybe hosted on the server of the vendor in or outside India. The contract allows the customer to access the site and enjoy certain privileges. This would be clearly under service tax.
14. Online access and retrieval: There are certain content sites like Bharat Matrimony, TaxIndia online etc which provide facility of accessing their sites for a period and allow one to read at times download. Since there is no transfer of property though one has a right to see or download at times it maybe a service.
15. Sharing of IT infrastructure costs: At times the group of companies under the same management invest in a central facility and utilise the same for all the companies. This is a joint expenditure shared by all constituents. It can be considered as a reimbursement of costs which maybe by way of allocation. May not be liable to either VAT or ST.
16. Music / Video / Games on Mobile: Where the transfer takes place it would be liable to VAT. However if it is online access it may only be liable under service tax.
17. Instant messaging, social networking: These maybe considered as services. At times these are personal in nature.
18. Maybe more...