



Implications of change in rate of tax for ongoing works contracts

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The Union Budget increased the rate of Service Tax 12.36% to 14% with effect from 01.06.2015. The 'Education Cess' and 'Secondary and Higher Education Cess' subsumed in the revised rate of Service Tax. The rate was increased to augment revenue and to prepare the tax payer for paying higher rate of tax in GST regime.

The emphasis of article is to bring out the clarity on rate of tax applicable for ongoing works. Before going further it is very interesting to note that past history on 'applicable rate of service tax'. It was settled position of law that taxable event in case of service tax law is date of rendition/provision of service.

Revenue department in couple of cases raised the demands based on date of receipt of amount or based on date of issuing invoice ignoring the vital fact that the service provided was when the existing rate of tax/exemption prevalent. Courts have held that taxable event in case of service tax law is rendering the service and service provider is liable for service tax @ rate prevalent on date of rendering service. Date of invoice & date of receipt of money shall not alter the tax liability.

- Contractor Association (Civil) Rajasthan Rajya Vidyut Mandal 2013 (32) S.T.R 396 (Raj)
- Vistar Construction (P) Ltd Vs UOI 2013 (31) S.T.R 129 (Del)
- Commr. Of Service Tax Vs Consulting Engineering Services (I) P. Ltd 2013 (30) S.T.R 586 (Del)

Then Central Government introduced the Point of Taxation Rules, 2011 prescribing date of issuing the invoice is deemed to be pointing time for determining liability of service tax. If the advance received prior to issuing the invoice, date of payment will be pointing time. Central Government had given utmost importance to date of issuing the invoice/date of receipt of advance rather than rendition of service for determining the pointing time for discharging the tax liability.

Again legislature intervened and introduced Section 67A with effect from 28.05.2012 which says:

- The rate of service tax,
- Value of a taxable service and
- Rate of exchange, if any,

shall be taken as the rate/value in force or as applicable **at the time when the taxable service has been provided or agreed to be provided.**

From the above it is clear that legislature itself had taken care of date of determining the tax rate. Which says date of determining the tax rate is date of rendition of service. Therefore legislative mandate of Section 67A is contradicting to what is specified in Point of Taxation Rules, 2011. Some High Court/Supreme Court has to resolve the incongruence between the Rules & legislative speech.

Till then it is duty of tax payer to follow the Point of Taxation Rules, 2011 as the tax administering department is keen on implementing POTR, 2011 to harvest more tax revenues.

Prior to 31.05.2015 tax rate was 12.36% & tax rate from 01.06.2014 is 14%. Service tax rate increased from 12.36% to 14%. Question is for particular transaction whether old rate-12.36% or new rate 14% applies especially in continuing contracts. In case of increasing/decreasing the effective rate of tax, Rule 4 of Point of Taxation Rules, 2011 explains whether old rate has to apply or new rate will apply. For better understanding the rule is explained with examples.. The same tabulated as follows:

Service provided	Invoice issued	Payment received	Rate
Before the change in rate of tax	After the change in rate of tax	After the change in rate of tax	14%
Before the change in rate of tax	Before the change in rate of tax	After the change in rate of tax	12.36%
Before the change in rate of tax	After the change in rate of tax	Before the change in rate of tax	12.36%
After the change in rate of tax	Before the change in rate of tax	After the change in rate of tax	14%
After the change in rate of tax	Before the change in rate of tax	Before the change in rate of tax	12.36%
After the change in rate of tax	After the change in rate of tax	Before the change in rate of tax	14%

Example

Service Provided before 31.05.2015

Invoice issued on	Payment received	Full Rate
10.06.2015	20.06.2015	14%
25.05.2015	10.06.2015	12.36%
10.06.2015	25.05.2015	12.36%
25.05.2015	30.05.2015	12.36%

Service Provided after 01.06.2015

Invoice issued on	Payment received	Full Rate
25.05.2015	20.06.2015	14%
25.05.2015	30.05.2015	12.36%
10.06.2015	20.05.2015	14%
10.06.2015	15.06.2015	14%

In case of typical ongoing construction contracts, service provider has to know the amount/quantum of service actually provided before 31.05.2015. The service provider has to prepare the documentation for the completed work and issue the invoice with service tax @ 12.36%. Invoice issued to customer may be running account bill (RA Bill) it does not matter. It is better to have to have Chartered Engineer Certificate evidencing the value of work completed.

If the service provider unable to issue the invoice dated prior 31.05.2015, he will end up paying the service tax @ 14% as in case of construction contracts, payment will be processed after submission of RA bill.

If the service provider receives any advance prior to 31.05.2015 before completing the work, by issuing the service tax invoice before 31.05.2015 service provider can pay the service tax @ 12.36%. It is irrelevant when the service is completed, service may be completed after 01.06.2015. If the service provider unable to issue the invoice dated prior 31.05.2015, he has to pay the service tax @ 14%.

Formula for better understanding- 2 out of 3:

From the above it can be understood that out of the 3 elements viz. (Date of issue of invoice, Date of payment and date of provision of service) if any of the 2 events occur before the

effective date of change in rate, then the old service tax rate shall be applicable. Since the new rate effective from June 1, 2015 therefore if any 2 events takes place before that then the benefit of old rate can be taken even after June 1, 2015.

For ongoing contracts where agreement provides reimbursement of service tax @ 12.36% and the work is continuing after 01.06.2015, service provider with suitable letter can ask the receiver to reimburse the difference in tax as service tax is destination based consumption tax, consumer has to bear the tax component. Otherwise service provider has to bear burnt of increased service tax.

In case of future contracts, service provider has to ensure at the time of entering agreement escalation has been suitable provided for safeguarding loss against increase in rate of tax by the Government in coming years.

GST rate may be around 18 to 24% maybe by 2017. In such a scenario every ongoing contract has to provide the escalation in respect of increase in taxes. Otherwise profit margin earned in particular contract will not be sufficient for paying the increased tax liabilities.

Please reach us at anil@hiregange.com for any further clarifications/ suggestions / feedback.

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