



Value Addition – Service Tax

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In the recent times we have seen margins getting squeezed and competitiveness increasing. Indirect tax constitutes around 25-30% of the top line in most manufacturing

industries and 10-15% in Services. Indirect Tax laws are unfortunately different in their applicability and there are a number of restrictions on the credits in respect of capital goods, inputs and input services. Tax laws in India are ever changing and quite complicated. The tax administrators as well as the Internal Audit Parties/ CAG teams are becoming more demanding as they are unable to reach the stiff targets set by the FM & CBEC. Now Scrutiny instruction given under central excise as well as service tax may add to the service provider's burden under this self assessment scheme!!

“Tax optimization” needs to be differentiated from tax evasion wherein one suppresses recording his sales/ services or undervalues the same deliberately. Tax optimization involves the arrangement of one's affairs in a way in which one can pay the least amount of tax or gets the maximum out of it.

In India IDT accounts for double the DT if one were to add VAT. In this material, an attempt has been made to touch on some possible areas of tax optimization under Service tax.

Tax Optimization - Impact under Service Tax

Tax optimization under service tax can be an arrangement of financial activities in such a way that maximum tax benefits, as provided in the provisions of Service Tax and Rules made under are availed to the assessee. It envisages use of certain exemption, selections of valuation method, structuring the transaction and selection of various benefits available under the law.

Few of such Tax Optimization tools having impact under Service Tax are as follows:

1. Drafting of the Agreement:

Drafting of the agreement would play an important role in determining the taxability aspect of the entity under Service Tax. The drafting of the agreement should be done after considering the

Customer profile, Vendor understanding and all the facts of the case which would be result in reduction in payment of Service Tax on the manufacturers. For example drafting of Agreement in a proper manner for employees recovery for termination fees, commission from vendor, may result in non applicability of Service Tax. Hence, for each and every case, the manufacturer requires to analyze the facts and appropriate tax planning can be done at the drafting of the agreement which may result in decrease of tax burden.

2. Tax Planning in case of Works Contract:

If the manufacturer is engaged in providence of Works contract service along with sale of goods, then the manufacturer should ensure that adequate bifurcation in the purchase order is being done in quotation for determining the value of the Service. If such bifurcation is not available, then the manufacturer would end up paying the Service Tax liability as per the Service Tax Valuation Rules, 2006 which may end up in payment of higher amount of Taxes.

3. Selection of vendors:

As explained above, under new Service Tax law w.e.f 01-07-2012 ST, the concept of Joint charge is introduced where the Service Tax would be payable by both Service receiver and Service provider if the Body corporate has taken specified service from Individuals / Firms. The manufacturer who is a body corporate can examine the selection of vendors who is other than individual / firms so that there would be no impact of Joint charge liability and additional compliances under Service Tax.

4. Standard Operating Procedure for availment of Cenvat Credit:

CENVAT Credit on Input Services plays important role in determining the profitability to the manufacturers. Hence, in the initial state itself, manufacturers require to have a proper system for availment of CENVAT Credit on all the eligible Input Service Credits. Eg: Many manufacturers were not availed the CENVAT Credit on the Service Tax liability under Reverse charge and still many are thinking that CENVAT Credits paid under Joint charge is not eligible. To clear these ambiguities, if the proper system / Standard Operating Procedure are implemented, then there would not be less scope for loss of credits. Further, the manufacturer also eligible to avail the CENVAT Credit on the CHA Service paid at the time of Import.

5. Tax Planning for SEZ Manufacturer:

There is an exemption available to the SEZ manufacturer from the Service Tax by way of following two options.

- A). Exemption by way of refund on Input Service Tax paid to the vendor.
- B). Exemption from the payment of Service Tax for the service taken at initial stage.

The notification issued contains separate procedure for claiming the exemption types mentioned above. Hence, the SEZ manufacturer should ensure that they follow the adequate procedures for claiming the outright exemption at the initial stage and the cost & procedures for applying the refund would be reduced.

6. GTA Planning:

As per the settled provision of law by virtue of many decisions, Service Tax would not be applicable for Goods Transport Service taken from the Goods Transport Operator rather the liability would be attracted if and only if Services has taken from Goods Transport Agency. Hence, manufacturer should ensure that if feasible, transport services to be taken from the Goods Transport Operator than Goods Transport Agency.

Further, entry no. 21 (b) & (c) of exemption notification no.25/2012 ST exempts Goods Transport Agency Service in a single consignment less than one thousand five hundred rupees and Rs. Seven Hundred and Fifty in a single carriage. The manufacturer should ensure that he has considered the above exemption in the payment of Service Tax on GTA Service.

7. Leasing of Machinery:

Under the old Service Tax law, supply of Tangible Goods service was introduced where the leasing of Machinery / equipments without *transfer of control and possession* would be liable for Service Tax. The same proposition continued under the new Service Tax law. Hence, drafting of agreement plays a vital role in substantiating this fact to the department and payment of Service Tax. So, it is advisable to the manufacturers to clearly mention in the agreement on this aspect so that there would not be any confusion and would not lead to double payment of both Service Tax and K-VAT on the same transaction.

8. Re-imburements:

The decision of the Hon'ble Delhi Court in the decision of M/s Intercontinental Consultants & Technocrafts Pvt Ltd Vs Union of India 2013 (29) STR 9 (Del) held that actual reimbursements recovered at cost are not liable for Service Tax. Hence, if the customer is not in a position to avail the CENVAT Credit, then the manufacturer would examine the option of not to charge the Service Tax on reimbursements claimed at actual. Further, if the manufacture is having an accumulation of credits, then he can also instruct the vendor not to charge the Service Tax on reimbursements. However, proper disclosure to the department is necessary in this regard to the department.

9. Input Service Distributor & Centralized Registration:

If the manufacturing is having a more than one manufacturing unit at different places and receives the input service bills like Audit fees, bank charges to the one unit, then in such cases, the manufacturer can claim the entire amount of credit in the unit which receives the bill and the proportion of the credit pertaining to other branch to be distributed via ISD route. It helps the manufacturer in reducing the risk of accumulation of credits in one unit.

Further, if the manufacturer is having the marketing office and other branches at other places, then the same can be registered as under Centralized registration and the credits can be taken under the main branch leading to proper avilment of all the credits.

10. Job work exemption:

As explained earlier, if the manufacturer avails the exemption under notification no.25/2012 for the Job work activity, then the transaction would be treated as Exempted Service and there may be applicability of Rule 6 of CENVAT Credit Rules, 2004 and would result in loss of Credits pertaining to the Job work Income. Hence, if the customer is in a position to avail the CENVAT Credit, it is better to the manufacturer not to claim the exemption.

11. Other Measures

Apart from the above following are additional techniques which may be followed:

- ➔ Vendors / Customers Education to optimise credits.
- ➔ Proper Training and Awareness to employees in purchase and sales.
- ➔ Reconciliation at Regular Intervals.
- ➔ Internal Audit to Include Service Tax.

- **Minimize the disputes and costs of litigation** - Being clear on what one is doing avoids the sapping of resources as well as at times confidence of the person.
- **Minimize the possibility of revenue audits** - [pay in time and file returns in time] Once audit is fixed minimize the time of departmental audit cost [interest/ penalty] by being ready.
- While interpreting laws to ones advantage, practice the policy of **full disclosure** in acknowledged disclosure to avoid charges of suppression and consequent penalty and longer period demands.
- **Be updated to take advantage of changing laws** - The recent high court decisions on reimbursement of expenses not being taxed, chit funds being out of net, accommodation, supply of food by hotels not being taxable under service tax are examples of proactive change in billing.

Conclusion: The above possible value added list is only illustrative and for each and every transaction there is a possibility of further Tax Planning and Cost Control. However, there is no hard and fast rule for this and the same is depending on the facts and circumstances of each case. Further, these policies should be reviewed at the regular intervals to equip with latest developments under all indirect tax laws such as Central Excise, Customs and VAT which could all have an impact on service tax.