

Impact of imposition of Swachh Bharat Cess: FAQs

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This festive season, service sector has witnessed imposition of Swachh Bharat Cess (SBC) in very hasty move by government. It was promised at the time of the budget that it would only be imposed on some services. Govt has gone back on its word. Further they have been left with very little time to prepare for this new tax. This owed to lack of clarity over various issues, holiday period and limited time between issuance of notification for levy and actual levy. Trade and industry had insisted for deferring the levy, but the government has ignored to such demands as is its past practice (ease of doing business, having certainty has been given a go bye) and consequently the SBC has become effective from 15.11.2015.

Board had issued Notification No. 21/2015-ST to 25/2015-ST addressing various aspects on SBC. They have also come out with FAQ dated 14th November, 2015.

We have analysed key issues arising out of imposition of new levy and presented in FAQ format.

1. Whether SBC is applicable to all the Services?

Initially there were indications that SCB would be imposed on few selected services. But the notification issued by government has provided that it shall apply on all the services except the one which are covered under the negative list or exemption notification.

2. Services are covered by mega exemption notification i.e. 25/2012-ST. Whether SBC would be applicable on such services?

No, it has been specifically provided in the Notification No. 22/2015 that SBC would not be applicable on services exempted from levy of service tax. Hence, SBC would not be applicable on the services covered by mega exemption notification. Similar would be treatment of negative list services.

3. Whether SBC is applicable on services rendered in J&K/non taxable territory?

Preamble to Chapter V of the Finance Act provides that provision of this chapter (i.e. chapter V) does not extend to J&K. SBC is levied under chapter VI of the Finance Act, 1994 where there is no specific mention about territorial application. However, section 119(5) provides that provision of chapter V of the Finance Act in relation to levy and collection of service tax shall equally be applicable to SBC also. Based on this, it can be said that SBC shall not have applicability in J&K/Non taxable territory.

4. Whether SBC would be levied on the services provided to SEZ unit/developer?

Services provided to SEZ unit/developer is exempted from service tax leviable under section 66B vide notification no. 12/2013-ST. There is no consequential amendment in the said notification. Hence, technically, service provider engaged in providing services to SEZ units would be liable to charge SBC on the invoice issued to SEZ unit even though not liable to service tax if covered by exemption notification 12/2013-ST. Similar would be treatment where services received by SEZ unit is covered by RC/JC.

However, this may not be intention of government to levy SBC on services provided to SEZ in view of the exemption granted from SBC on services covered by mega exemption notification/negative list. Representation should be made to government for issuance of suitable notification granting exemption from levy of SBC.

5. What would be effective rate of service tax post introduction of SBC?

Effective rate of service tax post introduction of SBC would be 14.5%.

6. Whether SBC would be applicable on services covered by Rule 6 of Service Tax Rules (i.e. air travel agent, insurance premium, purchase-sale of foreign currency)

Yes, as clarified in Notification No. 25/2015, SBC would be applicable on such services also. SBC would be determined by multiplying total service tax liability calculated under sub-rule (7), (7A), (7B) or (7C) of rule 6 by 0.5 and dividing the product by 14 (fourteen)

7. In case of services covered by abatement, what would be effective rate of tax? Say GTA service where presently tax is payable at 4.2% (14%*30%)?

*As clarified in Notification No. 23/2015-ST that in case of services covered by abatement notification, SBC would be calculated on net taxable value after claiming abatement. Hence, the effective rate of tax on all abatement services would be 14.5% * effective rate under Notification 26/2012-ST. For GTA, it would be $14.5\% * 30\% = 4.35\%$ ($4.2\% + 0.15\%$)*

8. In case of works contract, how would the tax be calculated?

*The value of services would be calculated as per Rule 2A of Service Tax (Determination of Value) Rules, 2006. Tax needs to be applied on the value so arrived at the rate of 14.5%. Effective rate of tax in case of original works and other than original works would be 5.8% ($14.5\% * 40\%$) and 10.15% ($14.5\% * 70\%$) respectively. Similar, would be for restaurant ($14.5\% * 40\%$) and outdoor catering services ($14.5\% * 60\%$).*

9. If services have been provided prior to 15th November but invoiced on or after 15th November, whether SBC would be applicable? (no advance received)

The rate of tax is determined as per section 67A which provides that the rate of tax would be applicable as on the date on which service is provided.

As per the philosophy in CCE vs. Vazir Sulthan Tobacco Co Ltd (1996(83) ELT3 (SC) that there cannot be any tax liability if taxable event happen before introduction of levy. The logic which can be inferred from this decision is that if services were provided when the services were taxed to service tax at 14%, then SBC need not be paid thereafter on such services either. Hence, SBC would not be applicable on services rendered pre 15.11.2015.

10. Is there any conflict between section 67A and Rule 5 of the Point of Taxation Rules, 2011 (PoTR)?

Section 67A provides that rate of service tax shall be the rate which is in force or applicable at a time when taxable services have been provided or agreed to be provided. If one follows this provision, then SBC shall not be applicable in respect of services provided before 15.11.2015. The timing of raising of invoice or receipt of consideration become inconsequential.

Clause (a) and (b) of Rule 5 of Point of Taxation Rules, 2011 (applicable for SBC as clarified by Board) begins with phrase "no tax shall be payable". This rule does not determine point of taxation in case of new levy but provides relaxation from levy on fulfillment of specified conditions.

The rule provides that no tax shall be payable to the extent invoice issued and payment received before service is taxed for the first time. Also the rule relaxes the requirement to issue invoice and provides that no tax shall be levied where payment received before service become taxable and invoice issued within 14 days of levy.

This could be understood with following illustration:

Services completed on 10th November. Advances were received on 1st November but the invoice is issued on 2nd December (after 14 days of imposition of SBC). There would be no liability both as per section 67A and Rule 5 as the services have been rendered prior to levy

In another case where services have been rendered on 16.11.2015 but advance received on 1st November and invoice issued on 20th November. As per 67A, service tax shall be applicable as services have been rendered after levy but no tax shall be leviable as advance received prior to the date of levy and invoice issued within 14 days of levy. Thus, the rule provide relaxation from leviability of SBC.

11. What is relevance of Rule 2A of PoTR?

Rule 2A of PoTR defines date of payment. As per the rule, date of payment shall be the date of entry in the books of account or date of credit to the bank account of the person liable to pay tax, whichever is earlier.

However, in case of imposition of new levy, date of payment shall be the date of credit in the bank account provided such credit is AFTER 4 working days of new levy. This could be very crucial in managing the tax on transactions executed during transition period.

12. How would tax be levied during transition period?

For the services rendered prior to 15.11.2015, there would be no liability of SBC in terms of section 67A irrespective of timing of receipt of advances or issuance of invoice. For services rendered on or after 15.11.2015, following could be taxability under different scenarios.

| Date of credit in books of account | Date of credit in bank account | Date of raising of invoice | PoT | SBC applicable |
|------------------------------------|--------------------------------|----------------------------|--------------------------------------------------------------------|----------------|
| 10.11.2015 | 12.11.2015 | 17.11.2015 | 10.11.2015 (date of credit in <u>books of account</u>) | No |
| 12.11.2015 | 10.11.2015 | 17.11.2015 | 10.11.2015 (date of credit in <u>bank account</u>) | No |
| 12.11.2015 | 10.11.2015 | 30.11.2015 | 30.11.2015 (invoice raised after 14 days) | Yes |
| 14.11.2015 | 17.11.2015 | 17.11.2015 | 14.11.2015 (payment received within four days of new levy) | No |
| 14.11.2015 | 20.11.2015 | 17.11.2015 | 20.11.2015 (as payment received after 4 working days from of levy) | Yes |
| 10.11.2015 | 17.11.2015 | 14.11.2015 | 10.11.2015 (payment within four days of levy) | No |

One could follow above indicative table to manage tax liability by ensuring that date of payment on or before 19.11.2015 and invoice issued on or before 29.11.2015.

13. I am paying service tax on few services under reverse charge mechanism. How would SBC have impact on my tax liability?

SBC would be applicable on all taxable services. Hence, you need to pay SBC along with service tax on the services availed by you.

14. How would liability be determined in case of reverse charge services where services have been received prior to 15.11.2015 but consideration paid post 15.11.2015?

Rule 7 of PoTR is applicable in case of RC/JC cases where liability arises on the date of payment to service provider. However, in respect of services received before 15.11.2015, there may not be any liability under RC/JC even if payment is made post 15.11.2015 as there was no levy in terms of section 67A when the services were rendered. But department could contend that liability arises on the date of payment and hence may demand payment of SBC.

15. Whether SBC needs to be collected and paid separately from service tax or subsumed in existing service tax rate?

SBC would be levied, charged, collected and paid to government independent of service tax. This needs to be charged separately on the invoice, needs to be accounted separately in the books of account and needs to be paid separately under separate accounting code which should be notified separately.

16. Whether SBC paid on input service would be eligible as credit?

There is no amendment in the Cenvat Credit Rules, 2004 regarding availment and utilisation of SBC. In the absence of the same, credit may not be admissible. (Are we really moving toward GST regime where there would no cascading effect of taxes and full credit would be allowed?) One can expect that suitable amendment is brought in Cenvat Credit Rules, 2004 to provide for availment and utilisation of SBC.

Tax payers should actively seek that the allowability of credit is made clear.

17. What is the rationale behind not including SBC in the CENVAT Chain?

The SBC has been levied to fund Swachh Bharat Program of GOI. By not allowing credit of SBC, the government would be able to raise multiplier funds. It is just a revenue augmentation exercise to whip the running horse.

This is certainly against the basic philosophy of Value Added System of taxation which allows for levy of tax only on value addition. Where the industry has been looking at government to support them in the environment of economic sluggishness and anticipating herald of near perfect GST, this move has really added to the woes of industry and has raised doubt as to intent of tax reforms by government in present tax regime as well as upcoming GST.

The impact of imposition of SBC could be visible in the cost of goods and services which may increase in the range of 0.5-2% (could be even more) due to non admissibility of credit.

18. Whether service provider could contemplate availing credit based on some judicial precedence?

There has been judgment of Karnataka High Court in case of Shree Renuka Sugars Ltd (2014-TIOL-98-HC-KAR-CX) where question had come before HC as to whether credit of sugar cess levied under Sugar Cess Act be allowed considering it in the nature of duty of excise. It has been held by High Court that sugar cess paid is credited to Consolidated Fund of India. Hence, it ceases to be in the nature of cess or fee and partakes the character of duty or a tax. Once it is considered as duty, Cenvat Credit would be eligible even if there is no specific provision in the Cenvat Credit Rules to allow credit for the same.

The rationale may be applied to SBC also as the proceeds of SBC would be first credited to Consolidated Fund of India and appropriation shall be made therefrom.

One could evaluate taking credit relying on above judgment. The same may be availed and reversed under protest each month till judicial clarity emerges.

19. What would be impact of imposition of SBC on cost of goods and services?

As per the present scenario, in the absence of any notification providing for availment of credit of SBC, it would directly add to the cost of product and services. If you are manufacturing excisable goods, you will have to factor in additional cost of 0.5% on all services received by you in the course of manufacturing. Similarly, if you are providing taxable service, SBC paid on all your input service become cost. If you are exporter of goods or service, you will not be entitled for refund of SBC, which was paid on eligible input services used for export of goods.

20. What would be impact of imposition of SBC on cash flow of service provider?

Imposition of SBC would have negative impact on cash flow of service provider both on procurement and supply side. There would be additional cash outflow upto 0.5% on procurement of services. Moreover, one may not be able to utilize the credit of service tax/excise otherwise available with them for payment of SBC resulting in additional cash outflow on supply side. There could be situations where service providers may have huge credit balance with them yet they will have to pay the SBC in cash.

21. I am providing both exempted and taxable service and reversing credit @ 7% of value of exempted service under Rule 6 of Cenvat Credit Rules? Do I need to reverse the SBC also?

SBC would be levied and collected as service tax. Reversal under Rule 6 is not payment of "service tax" but it is payment of "amount". Hence, reversal of SBC is not required under Rule 6 of Cenvat Credit Rules, 2004.

22. I am a service exporter. How can I claim back SBC paid on my input service.

A service exporter may get back the taxes paid on expenditure incurred by him by claiming refund of Cenvat Credit under Rule 5 of Cenvat Credit Rules or rebate under Notification No. 39/2012-ST. Claiming benefit of SBC under these provision could be as follows:

Refund under Rule 5 of CCR: SBC may not be granted as refund by department as it has not been entered into cenvat chain.

Rebate under Notification No. 39/2012-ST: Rebate could be claimed as rebate of cess has been specifically mentioned in the notification without mentioning the nature of cess and hence a possibility may be explored for claiming the rebate.

23. I am an exporter exporting goods outside India. Can I claim benefit of SBC?

An exporter may claim benefit of service tax paid on input services/specified services as follows:

Refund under Rule 5 of CCR: SBC may not be claimed as SBC has not been entered into cenvat chain.

Rebate under Notification No. 41/2012-ST: There is no specific mention in the notification that the rebate would be granted only of service tax levied under section 66B. Hence, the possibility of claiming rebate may be explored under this notification

24. A Residential Welfare Association (RWA) has received maintenance charges for the month of November in advance. Do they need to raise supplementary invoice to collect SBC for the maintenance charges pertaining to period post 15.11.2015.

No, if advance has been received before levy of SBC and invoice issued on or before 29.11.2015, there is no need to collect SBC by raising supplementary invoice. Hence, RWA need to ensure that invoice is issued on or before 29.11.2015.

25. I had purchased a flat in respect of which demand letter has been received from builder on 1st November, 2015 for milestone payment based on terms of agreement. I have not paid the installment yet. Now the builder is demanding SBC also. Whether it is correct?

Issuance of demand letter by builder indicates that the services had been completed to the extent demand made based on the agreement between parties. As the services were completed prior to levy of SBC, there is no liability of SBC even if installment is paid now. The action of builder to demand SBC is not correct.

26. I am executing ongoing contracts where billing is done in end or date after the date of SBC imposition- what can I do?

One could estimate the value of the service already provided and raise a bill for service provided till 14.11.2015. As service is provided and bill raised, the rate would be only 14%. This would also avoid any issues with the revenue. If not possible intimate the revenue on the work completed and the decisions where rendition of service has been held to be required for imposition of ST and then at the time of billing bifurcate between the service provided prior to and after 15.11.2015.

27. In case I have charged SBC and later the consideration is re-negotiated due to deficiency in provision of service, where the excess SBC paid to that extent, whether can be adjusted?

Rule 6 (3) of Service Tax Rules provide for taking credit of tax paid in excess where such excess payment is on account of (i) a service to be provided which is not so provided by either wholly or partially for any reason, (ii) or where the amount of invoice is renegotiated due to deficient provision of service or (iii) any terms contained in a contract provided credit note is issued by service provider or refund made.

SBC would also be levied as if it is service tax. Hence, above provision would equally applicable to SBC also and you will be entitled to adjust the excess amount paid against future liability.

Conclusion

In the certainty of law remains the safety of the citizens. Too many changes lead to unintended mistakes which are then leading to unnecessary demands and costs.

Though the objective of the collection of specific cess for a Swachh Bharat Mission is appreciable, the psychological impact on common man would be high with increased burden of taxes. This is especially with the fact that there is no provision for credit (unless it is provided for) and also additional burden on the business man to keep track of the one more tax, as to invoicing, record keeping, payment and returns filing.

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It appears that the movement to mop up taxes in bits and pieces at different times along with the delayed and diluted of the GST in its pristine form does not indicate that the executive would allow the real "ease of doing business" to happen.