

TAX LIABILITY UNDER “REVERSE CHARGE MECHANISM” AND “JOINT CHARGE MECHANISM”

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INTRODUCTION

- Service Tax is a Vital Part of Indirect Tax Structure.
- It can be spelled as tax on specified services provided by the Service Provider.
- Usually the person providing the Services is liable to pay Service Tax but here comes an exception, where service provider is not liable or is partially liable to pay service tax and the recipient has to bear the liability to pay the tax on behalf of the service provider.
- This concept is known as :-
 - Reverse Charge Mechanism and
 - Partial Reverse Charge Mechanism

Sr. No.	Nature of Service	Service Provider	Service Recipient	Rate (Provider)	Rate (Recipient)
1.	Insurance Agent Services	Any	Any	Nil	12.36%
2.	Transportation of Goods by road	GTA	6 Category Specified	Nil	3.09%
3.	Sponsorship Services	Any	Firm or Company	Nil	12.36%
4.	Import of Services	Any	Any	Nil	12.36%
5.	Advocate Services	Individual / Firm / LLP	Any Business Entity	Nil	12.36%
6.	Support Services by Govt. & Local Authority	Govt. or Local Authority	Any business Entity	Nil	12.36
7	Renting of Motor Vehicle	Individual / HUF / Firm / AOP	Company	7.416% (In case of abated)	4.944%

Sr. No.	Nature of Service	Service Provider	Service Recipient	Rate (Provider)	Rate (Recipient)
8.	Supply of Manpower	Individual / HUF / Firm / AOP	Company	3.09%	9.27%
9.	Works Contract (New construction)	Individual / HUF / Firm / AOP	Company	2.472%	2.472%
10.	Works Contract (Repair/Maint - Goods)	Individual / HUF / Firm / AOP	Company	4.326%	4.326%
11.	Works Contract (For Immovable Property)	Individual / HUF/Firm/ AOP	Company	3.708%	3.708%
12.	Works Contract (Tax on Labour portion)	Individual / HUF / Firm / AOP	Company	6.18%	6.18%
13.	Services by Director	Individual	Company	Nil	12.36%

Services under Reverse Charge

1. Insurance Agent Service:-

- **Applicability:-**

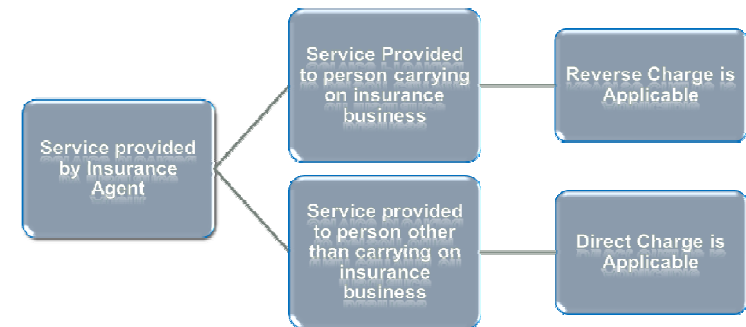
Insurance agent providing services to a person carrying on insurance business.

- **Analysis:-**

- Relief from service tax compliance to the extent of income receivable from person carrying on insurance business.
- Service tax are required to be discharged by the agent as service provider on the income other than above, earned by such agent.

- **As per Rule 9 Place of Provision of Service Rules, 2012**

- Insurance Agent - located in Non Taxable Territory – service is considered as non Taxable.
- Insurance Agent - located in Taxable Territory – service is considered as Taxable.



2. SPONSORSHIP BUSINESS

- **Applicability:-**

Sponsorship services provided to any Body corporate or Partnership firm located in taxable territory.

- **Service Tax Liability:-**

▪ Service receiver is a body corporate or partnership firm located in taxable territory-	Entire tax payable by service receiver
▪ If the receiver of service is not body corporate or partnership firm or if such body corporate or partnership firm is not located in taxable territory	Entire tax is payable by service provider.

3. Legal Services/Services by advocate

- **Applicability:-**

- Services provided to business entities, with a turnover exceeding Rs. 10,00,000 in the preceding financial year, tax is required to be paid on reverse charge by the business entities i.e. service receivers.

- **Exemption:-**

Legal services provided by advocates or partnership firms of advocates are exempt from service tax when provided to the following:

- An advocate or partnership firm of advocates providing legal services
- any person other than a business entity
- A business entity with a turnover up to rupees ten lakh in the preceding financial year.

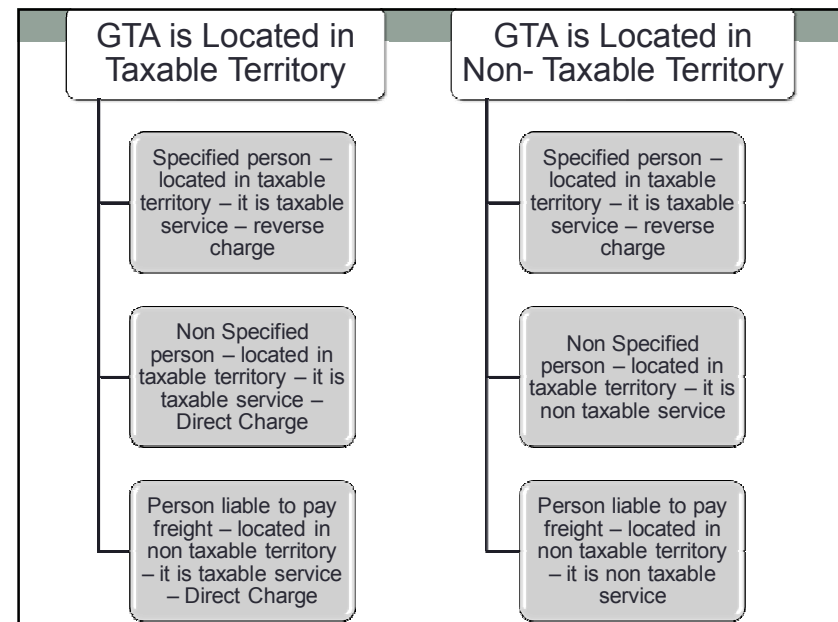
4. Goods Transport Agency

Applicability:-

Service provided by a goods transport agency in respect of transportation of goods by road, where the person liable to pay freight is,—

- Any factory registered under or governed by the Factories Act, 1948
- Any society or a co-operative society
- Any dealer of excisable goods, who is registered under the Central Excise Act, 1944
- Any body corporate, or
- Any partnership firm whether registered or not, including association of persons;

Provided by that when such person is located In a non-taxable territory, the provider of such service shall be liable to pay Service Tax.



Analysis

Taxability

- 75% Abatement on the Service Amount say On Rs 100
- Taxable Amount Rs.25

Liability

- Recipient Liable to discharge ST
- Any person who pays freight either himself/Agent

Place of Provision

- POP of services of GTA shall be the Location of Person liable to pay tax.
- Provided that when the person is located in Non Taxable Territory, the provider shall be liable to pay ST

Exemption from Service Tax for GTA

- Transportation of fruits, vegetables, eggs or milk by road in a goods carriage
- No Service Tax is to be paid when Gross Amount charged on all consignments transported in a goods carriage does not exceed Rs. 1500/-
- No Service Tax is to be paid when Gross Amount charged on individual consignment transported in a goods carriage does not exceed Rs. 750/-
- Taxable value of Goods Transport Agency Service shall be exempt in excess of 25%. In other words, abatement of 75% is available.
- Services tax paid on service provided for transport of goods from inland container depot to the port of export can be claimed as refund.

5. Support Services by GOI

- Support Service provided by GOI or Local Authority except:-
 - Renting of Immovable Property
 - Services specified under Section 66D Entry (a) of the Finance Act, 1994, which are:-
 - Services provided by Department of Post Office like Speed Post
 - Services in relation to Vessel or Aircraft
 - GTA or Passenger Transport Service

To any business entity located in the taxable territory, the recipient of such service.

Analysis

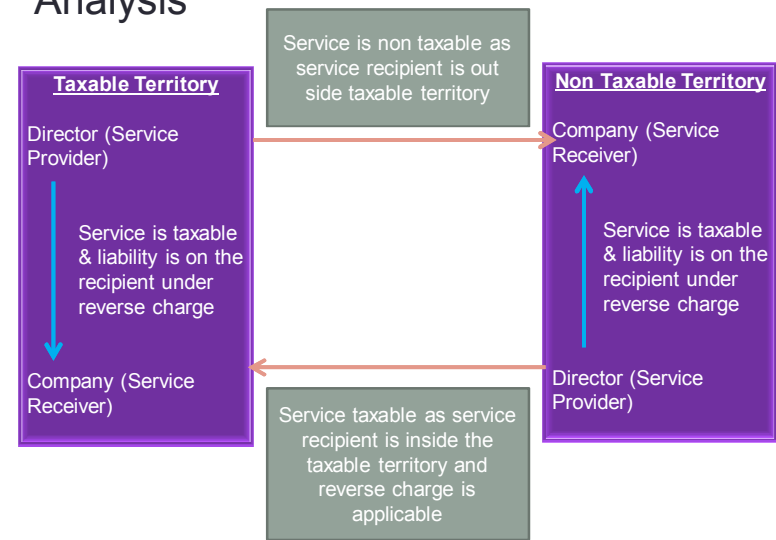
Support Services provided by GOI or Local Authority	
Type of Service	Taxability of Service
Renting of Immovable Property	Direct Charge
Services Specified in rule 66D	Direct Charge
Any other support service provided to business entity located in Taxable Territory	Reverse Charge is applicable
Any other support service provided to other than business entity.	Service tax is not applicable as per "Negative List"

6. Director Services

• Applicability:-

- In relation to services provided by or agreed to be provided by a director of a company to its company, the recipient of such service.
- All payment against services including part time Director's remuneration, director's setting fees, commission etc., receivable from company to the director have been subjected to service tax.
- Service tax is not applicable where employer employee relationship is existing therefore any sum paid to whole time director is not liable to tax.

Analysis



7. Import of Service

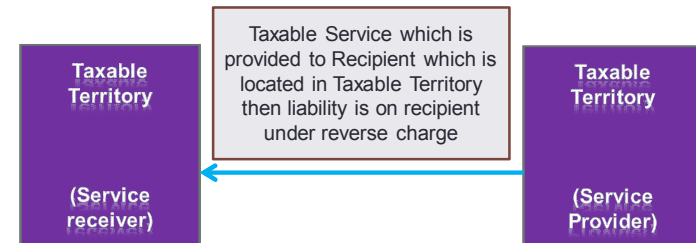
• **Applicability:-**

In relation to any taxable service provider or agreed to be provided by any person which is located in a non-taxable territory and received by any person located in the taxable territory, the recipient of such service.

For the purpose of this service,

- “Taxable Territory” means the territory to which the provisions of this chapter apply i.e. India excluding the State of Jammu & Kashmir.
- Even if the Service Provider is located outside taxable territory, the Service Tax is payable by recipient of Service.

Analysis

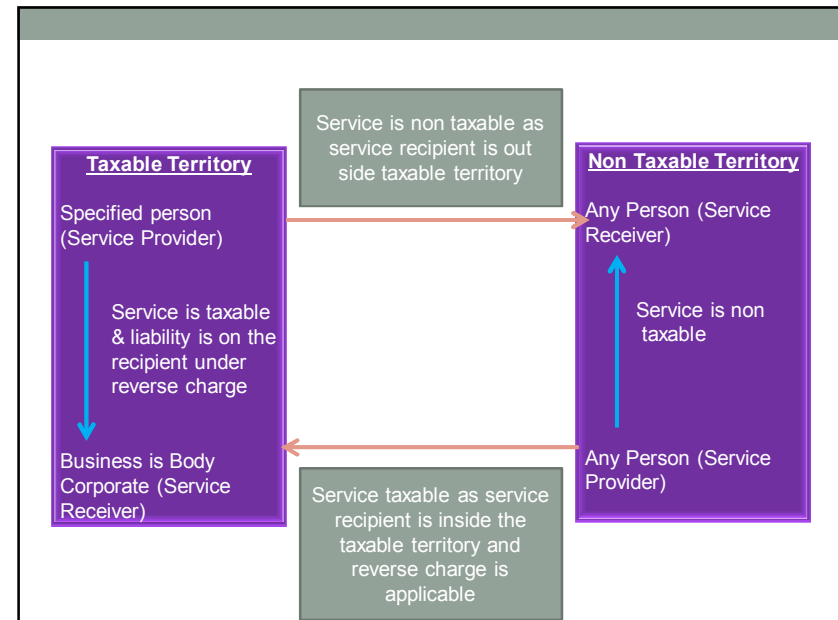


Services under Partial Reverse Charge

1. Manpower Supply Service:-

• Applicability:-

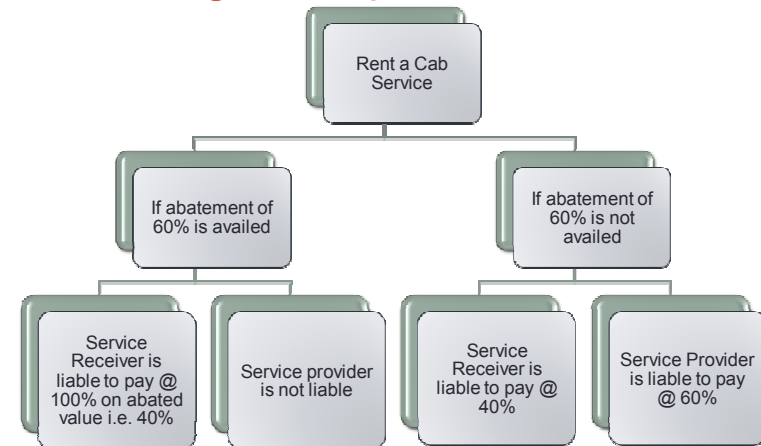
- In relation to services provided by way of supply of manpower for any purpose or security services by any Individual, HUF, Partnership Firm, AOP located in Taxable territory to a business entity registered as body corporate located in taxable territory, both the service receiver and the service provider to the extent notified in the Act.
- Supply of manpower means supply of manpower, temporarily or otherwise, to another person to work under his control.



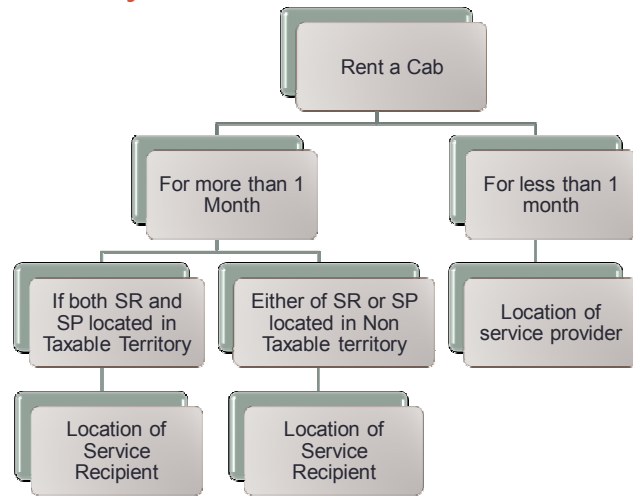
2. Rent a Cab

- **Applicability:-**
 - In relation to services provided by way of renting of a motor vehicle designed to carry Passenger
 - By any person who is not engaged in a similar business by any individual, HUF or Partnership Firm including AOP located in a taxable territory
 - To a business entity registered as body corporate, located in taxable territory, both the service provider and service recipient to the extent notified in the Act.

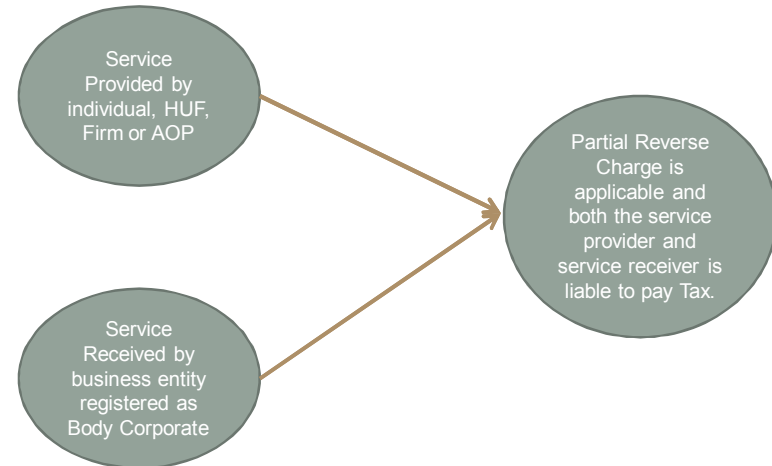
Percentage to Deposit



Taxability



3. Works Contract Service



Percentage to Deposit

- In case of works Contract Service-
 - Service Recipient is liable to pay tax @ 50%
 - Service Provider is liable to pay tax @ 50%

Taxability

Works Contract Service

Where SP and
SR is situated in
Taxable territory

Where any one is situated in non
taxable territory

As per rule 8
It is Taxable
Service

Service performed
on goods made
physically available

Where service is
provided from a
remote location

Location where
service is actually
performed

Location where goods
are located at the time
of provision of service

Details in Invoice under RCM

- Invoice shall indicate the name, address and the registration number of the service provider and person receiving taxable service; the description and value of taxable service provided or agreed to be provided; and the service tax payable thereon.
- As per clause (iv) of sub-rule (1) of the said rule 4A "the service tax payable" thereon' has to be indicated. The service tax payable would include service tax payable by the service provider.

Format Of Invoice

M/s MPS					
Labour Contractor					
To:					
M/s X Pvt. Ltd.					
Date:					
Invoice No.					Rs. Rs.
Assessable Value					10,00,000
(Being the charges for manpower supplied for the month of ____.)					
Add: Service Tax					
Rate (at)	12.00%	2.00%	1.00%		
	1,20,000	2,400	1,200	1,23,600	
Less: ST liability to be borne by SR in terms of Notification No., 15/2012 @75.00%					
	90,000	1,800	900	92,700	
Net ST Payable by SP	30,000	600	300	30,900	30,900
Total					10,30,900

Issues under RCM

- **Whether the Credit of Service Tax paid under RCM is eligible for CENVAT Credit??**

⇒ Normally, the credit of the entire tax paid on the service received by the service recipient subject to the provisions of the CENVAT Credit Rules 2004. The credit of tax paid by the service provider would be available on the basis of the invoice subject to the condition specified in the Rules. The credit of the tax paid by recipient under Partial RCM would be available on the basis of tax payment challan.

- **Point of taxation for service recipient.**

⇒ In terms of the Rule 7, point of taxation for the service recipient will be the date when he pays for the service.

⇒ **Example:-**

⇒ Date of Invoice – July 2012

⇒ Date of Payment – August 2012

Hence the point of taxation for Service Provider will be August 2012.

- **Is the reverse charge applicable on service provided or complete before 1st July, 2012 though payments were made after 1st July, 2012??**

⇒ For any service whose point of taxation has been determined and whole liability affixed before 01.07.2012 the new provisions will not apply. Merely because payments are being made after 01.07.2012 will not add any additional liability on the service receiver in respect of such services.

- **How to compute quantum of tax liability?**

⇒ *To be carried out in four steps:*

First step – The first step will be to compute tax liability by the SP in respect of each service rendered. It means that the SP will have to determine ST liability with respect to each invoice issued.

Second step – In the second step, invoice to be raised will contain total tax liability in respect of the particular invoice and apportionment of the same as provided.

Third step – In the third step, since the SP will be providing the same type of services to all the SRs, balance amount of ST as appearing in various invoices will be his total tax liability.

Fourth step – In the fourth step, amount of the CENVAT credit for which he is entitled to will be deducted from the total tax liability as determined under third step.

• **Computation of tax liability of Service Receiver**

⇒ **SR liable to pay ST on receipt of invoice from SP** – On receipt of the invoice from SP, the SR will check its correctness and, if found in order, will have to discharge the same by making its payment before 5th of the next month. It should be noted that no deduction can be made by SR on account of CENVAT credit. SR will have to make payment of the entire amount of liability. On making of its payment, SR will be entitled to claim CENVAT credit in respect of the ST paid by him subject to the provisions of the CENVAT Credit Rules.

⇒ **When can SR claim credit of amount shown by SP in invoice** –

A question that may arise here is whether SR can claim credit for the amount of tax liability as appearing in the invoice of SP in the month in which invoice is received or in the month in which ST is paid?

Answer is:- No SR can not claim credit of amount shown by SP in invoice

• **CENVAT credit of SP and SR**

⇒ **Cenvat credit of SP** – A question may arise how to claim CENVAT credit of SP. In the above case (i.e. in Format of Invoice), ST liability of SP will be Rs. 30,900. For example, CENVAT credit entitlement of MPS is Rs. 25,000. In that case, ST liability of MPS will be Rs. 5,900 (i.e., 30,900 – 25,000). If CENVAT credit entitlement of MPS is, say, Rs. 35,000, net amount of ST liability of MPS will be Rs. *NIL*. An amount of Rs. 4,100 will be carried forward.

⇒ **An example** - As far as X Pvt. Ltd. is concerned, it can claim CENVAT credit of Rs. 30,900 in the month in which invoice is received. A question may arise with respect to Rs. 92,700, i.e., ST liability component falling on X Pvt. Ltd. Can it be claimed in the month in which the invoice has been received or after making payment of the same, i.e., next month.

⇒ It can be Claimed after Payment of the same.

- **SP's failure to discharge its ST liability**

⇒What will happen if in the above case MPS fails to discharge its liability of Rs. 30,900? Whether the ST Department can ask X Pvt. Ltd. to pay Rs. 30,900? **No**, as per the Notification, ST liability of X Pvt. Ltd. has been fixed at Rs. 92,700. Therefore, it cannot be asked to pay Rs. 30,900 pertaining to MPS. ST Department will have to recover Rs. 30,900 from MPS only. It cannot be recovered from X Pvt. Ltd.

- **SR's failure to discharge its ST liability**

⇒What will happen if in the above case X Pvt. Ltd. fails to discharge its liability of Rs. 92,700? Whether the ST Department can ask MPS to pay Rs. 92,700? **No**, as per the Notification ST liability of MPS has been fixed at Rs. 30,900. Therefore, it cannot be asked to pay Rs. 92,700 pertaining to X Pvt. Ltd. ST Department will have to recover Rs. 92,700 from X Pvt. Ltd. only. It cannot be recovered from MPS.

- **When SP would not be liable for ST**

⇒It may so happen that SP may be availing of basic exemption limit of Rs. 10,00,000. In that case he will not be liable to pay ST. A question that may arise whether, in that case, SR will be liable to pay ST? For example, in the above case assuming that MPS is entitled to basic exemption limit of Rs. 10 lakhs. Therefore, naturally it will not be charged ST. In that case, X Pvt. Ltd. will not have to pay any ST, even though it is a Pvt. Ltd. Co.

- **When SR would not be liable for ST**

⇒This is going to be the most difficult situation for various business entities. It may so happen that SR may not be covered under ST provisions, as they may not be providing any services. For example, an entity carrying on trading activities only. Let us take another case, that of an entity providing services total value of which is Rs 10 lakhs and, therefore, entitled to basic exemption.

(a) Whether SR will have to obtain registration under ST?

➤ Yes, SR will have to obtain Registration under ST

(b) Whether SR will have to file periodical ST return?

➤ Yes, SR will have to file periodical ST return

• **Issue of Invoice by SP**

⇒ This is going to be the most complex exercise. For which amount invoice is to be issued by SP? Should the amount received be considered as excluding tax liability of the SP and SR? In that case, both the SP and SR will have to pay following amount as ST :

Value of Service		100,000
SR, i.e., Y Pvt. Ltd. 75.00%	9,270	
SP, i.e., M/s PPF 25.00%		3,090
		<u>103,090</u>
Less: Advance Received		100,000
Balance to be received from Y Pvt. Ltd.		<u>3,090</u>

Example 1 – In this scenario, in addition to advance paid of Rs. 1,00,000, Y Pvt. Ltd. will have to make payment of Rs. 3,090 to M/s PPF and Rs. 9,270 to the Government to discharge its liability. Thus, it will be paying in all Rs. 1,12,360.

- **13.2 Example 2** – What will happen if Y Pvt. Ltd. insists on that it is not ready to bear any burden other than Rs. 1,00,000 already paid? In that case, the computation will be as follows :

Value of Service	89,000
SR, i.e., Y Pvt. Ltd. 75.00%	8,250
SP, i.e., M/s PPF 25.00%	<u>2,750</u>
	91,750
Less: Advance Received	<u>100,000</u>
Balance to be paid to Y Pvt. Ltd.	(8,250)

Example 3 – As can be seen from above, advance paid of Rs. 1,00,000 will result into tax liability of Rs. 8,250 for Y Pvt. Ltd. At the same time, it will have to recover Rs. 8,250 from M/s PPF. For obvious reasons, this may not be acceptable to Y Pvt. Ltd.

- **Two main issues** – There are two main issues, viz., loss of revenue and inconvenience to small business sectors. Let us examine each of these issues

⇒ **Loss of Revenue** – It is a fact that a large number of assessee who collect the tax and do not pay it to the Government. Many of them do not even file ST-3 return. Is this the remedy for solving the problem? What is the guarantee that the SR will pay the tax? Secondly, this provision covers limited number of companies as SRs. What about other cases of SRs wherein such things will continue to happen? Will they be permitted to occur?

⇒ **Inconvenience to small business sectors**

- They have limited resources – We have seen the problems involved and additional compliances required to be made by SRs. To what extent it is correct to presume that all the limited companies are large ones? There are hundreds of small businesses having corporate structure but which are small ones and having limited resources. Will this not add to their burden?
- How to check tax evaders – As all of us know, till the ST Department carries out in-house changes in its administration large scale evasion of tax will continue to take place. What is required is sincere efforts to catch the tax evaders. Have any serious attempts been made in that direction so far? ST Department is having data of all the registrants with it. It is a known fact that majority of them do not file ST-3 return. In how many cases notices have been issued for non-filing of return? In how many cases coercive actions have been taken to recover tax from defaulters and tax evaders?

Important points relating to RCM

- CENVAT can not be availed for discharging the ST Liabilities on RCM
- ST Paid under RCM can be utilize towards the discharge ST on output services
- Threshold exemption of upto Rs.10 Lac is not applicable here in RCM except Legal services
- Allowed Refund of unutilized CENVAT credit availed from input services as per Rule 5B of Central Excise Rules,2004

Accounting under RCM

Case 1

Where Service Tax has been charged fully in Invoice

		<u>Debit</u>	<u>Credit</u>
Expense A/c	Dr	100.00	-
Service Tax Input Credit A/c	Dr	7.42	-
Service Tax Deferred Input A/c	Dr	4.94	-
To Vendor A/c		-	105.42
To TDS Payable A/c		-	2.00
To Service Tax Payable A/c - Reverse Charge		-	4.94
		<u>112.36</u>	<u>112.36</u>

Case 2

Where Service Tax has not been charged in Invoice

Expense A/c	Dr	100.00	-
Service Tax Deferred Input A/c	Dr	12.36	-
To Vendor A/c		-	97.75
To TDS Payable A/c		-	2.25
To Service Tax Payable A/c - Reverse Charge		-	12.36
		<u>112.36</u>	<u>112.36</u>

Case 3

In case of Abatement (e.g. 40%)

		<u>Debit</u>	<u>Credit</u>
Expense A/c	Dr	100.00	-
Service Tax Input Credit A/c	Dr	4.94	-
To Vendor A/c		-	98.00
To TDS Payable A/c		-	2.00
To Service Tax Payable A/c - Reverse Charge		-	4.94
		<u>104.94</u>	<u>104.94</u>

