

## **Impact of Krishi Kalyan Cess- Service Tax**

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### **Introduction**

Service tax rate has been proposed to increase from 14.50% to 15% effective from 1<sup>st</sup> June 2016. It is also clear that till 1.6.2016, service tax shall continue to be levied @ 14.50% comprising of Basic 14.0% and 0.50% as Swachh Bharat cess (SBC).

It is proposed to be levied on any or all the taxable services at the rate of 0.5% on the value of such taxable services.

The purpose of levy of KKC on all taxable services is to finance and promote initiatives to improve agriculture. Credit of Krishi Kalyan Cess paid on input services shall be allowed to be used for payment of the proposed Cess on the service provided by a service provider. In other words, it could not be set off by the manufacturer against excise duty payable on final products which appears to be a poor draft as it would be used by scores of manufacturers.

In this backdrop, the paperwriters have examined the service tax implications of proposed Krishi Kalyan Cess(KKC) below.

### **Point of taxation and change in effective rate of tax**

Rule 2 (ba) of Point of Taxation Rules(PoTR) sets out that "change in effective rate of tax" shall include a change in the portion of value on which tax is payable in terms of a notification issued in the Official Gazette under the provisions of the Act, or rules made thereunder;

Rule 2 (e) sets out that the "point of taxation" means the point in time when a service shall be deemed to have been provided.

Rule 3 of PoTR sets out that point of taxation is earliest of following:

- a. Date of invoice or
- b. Date of completion of service or
- c. Date of receipt of advance.

Rule 4 of PoTR, is used to determine point of taxation in case of change in effective rate of tax. In a nutshell, the applicable tax rate would be the prevalent rate during the period when 2 out of the following three events have taken place namely: date of invoice or date of completion of service or date of receipt of advance.

## **Services Provided Earlier to 1.6.2016:**

### **Examples when old rate would apply**

- a. **Invoice raised before and payment received after 1.6.2016:** The invoice raised on 15<sup>th</sup> May 2016, and service provided in May 2016. Payment received in June 2016. The tax to be paid at 14.50% [old rate].
- b. **Where payment received before and invoice issued after 1.6.2016:** The invoice raised on 5<sup>th</sup> June 2016, and service provided in May 2016. Payment received on 30<sup>th</sup> May 2016. The tax to be paid at 14.50% [old rate].
- c. **When the invoice issued and payment received after 1.6.2016:** The invoice raised on 10<sup>th</sup> June 2016, service provided in May 2016 and payment received on 30<sup>th</sup> June 2016. The tax to be paid at 15.0% [new rate].

## **Services Provided Post 1.6.2016:**

### **Examples when old rate would apply**

- a. **Invoice raised and payment received before 1.6.2016:** If invoice raised on 5<sup>th</sup> May 2016, payment received on 15<sup>th</sup> May and service provided in June 2016. Then service tax to be paid at 14.5% [old rate].

### **Examples when new rate would apply:**

- b. **When invoice raised after 1.6.2016 and payment received before rate change:** If invoice is raised on 5<sup>th</sup> June 2016, payment received on 15<sup>th</sup> May and service provided in June 2016. Then service tax to be paid at 15% [New rate].
- c. **When invoice raised earlier to 1.6.2016 and payment made post change in rate:** If invoice raised on 15<sup>th</sup> May 2016, payment made on 1.6.2016. Then service tax to be paid at 15% [New rate].

## **Consequences of Change in Rate**

The immediate impact of the change in rate would be 0.50% increase in the payment by the service provider post 1.6.2016. Section 68(1) sets out that service tax is a levy which is

payable by the service provider. ST is a destination based levy, could be collected from the customer.

Service provider has statutory right to pass on the burden of the service tax component to service receiver in absence of prescription by legislature that service tax burden should not be passed on. The Finance Act, 1994 does not contain any such restriction that service provider should not pass on the burden to the service receiver.

However it also all depends on terms of contract between the parties. When the contracted price includes all taxes, then the increased service tax burden of 0.5% would go out of the pocket of the service provider. This is common in case of Govt contracts/contracts with PSU's /long term contracts.

When the terms of contract are in addition to price, all taxes including service tax extra as applicable, then the service provider could collect and pay the increased service tax. For all existing and future contracts, service providers engaged in providing taxable services to ensure they renegotiate and put in clause that 'taxes including service tax as applicable, to be collected extra from the customer'.

#### **Applicability of Krishi Kalyan Cess on on-going contracts are as under:**

- a) **Service Completed before 1.6.2016:** All the services provided upto end of May 2016 need to be billed. These would include those bills not raised which have been postponed, missed, other reasons. These are to be identified and bill raised by end of May 2016. Otherwise the 15.0% rate may have to be applied in future.
- b) **Part services provided before 1.6.2016:** The part bill to extent of completed service, could be raised before 1.6.2016 and service tax paid thereon by 5<sup>th</sup>/6<sup>th</sup> of June 2016 at 14.5%.
- c) **Advances received before 1.6.2016 for future services:** Even on advances received towards services to be provided in future, invoices to be raised by 30<sup>th</sup> May 2016 and ST could be paid at 14.5%.
- d) **Where the invoices are issued before 1.6.2016:** When the invoices are raised before 1.6.15 for services to be provided in future [post June 2016], service tax rate is 15.0%.

#### **Whether Krishi Kalyan Cess to be paid on Debtors as on 31<sup>st</sup> May 2016?**

In rule 5 of POTR, it is provided in two specified situations the new levy would not apply. Rule 5 specifically sets out that for point of taxation of services taxed for first time as under.

(a) no tax shall be payable to the extent the invoice has been issued and the payment received against such invoice before such service became taxable;

(b) no tax shall be payable if the payment has been received before the service becomes taxable and invoice has been issued within 14 days of the date when the service is taxed for the first time. The provision is silent about services which were provided before levy was introduced.

Another Explanation is being inserted therein by Budget 2016 stating that in situations other than those specified above, the new levy or tax shall be payable

In view of paper writer, this rule may not be valid. Section 66B specifies that the service tax is levied on the **services provided or agreed to be provided**. Section 67A(1) specifies that the rate of service tax shall be the rate of service tax in force or as applicable at the time when the taxable service has been provided or agreed to be provided. On a conjoint reading, the service tax is leviable at rate applicable at the point of time at which

1. the services provided or
2. agreed to be provided-advance receipt.

The logic which can be inferred, is that if services were provided or advance was received, when the services were taxed at 14.50%, then enhanced service tax need not be paid thereafter at 15% [including 0.50% KKC] either. It is to be paid at 14.50%.

In the past it was held in Delhi Chartered Accountants Society (Regd.) vs UOI 2013 (31) S.T.R. 429 (Del.) that invoice issued prior to 1-4-2012, when rate of Service Tax was increased from 10% to 12%. Payment received after 1-4-2012. Circular stipulating that in such cases also Service Tax had to be paid at rate of 12%. Held: Prima facie, Circular was in violation of Rule 4 of Point of Taxation Rules, 2011. In that case, the invoices were issued and service rendered prior to 01.04.2012.

The risk is that when services were provided earlier to 1.6.2016, service tax could be demanded at 15.0% [including 0.50% KKC] citing Rule 4 of PoTR, 2 out of three events namely raising of invoice and receipt of monies took place after change in rate. The service tax would be demanded to be paid at 15% [including 0.50% KKC] and not 14.50%.

The landmark judgement CCEE vs. Vazir Sulthan Tobacco Co Ltd (1996(83) ELT3 (SC) held that there cannot be any tax liability if taxable event happens 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 14.50%, then KKC need not be paid thereafter on such services either.

In respect of services where liability arises as receiver of service, the ST liability arises as on date of payment or where payment is not made within 3 months of invoice date. Then ST liability arises on next succeeding day after expiry of 3 months. The rate applicable at the point of time, when ST liability arises is to be considered. Section 67A sets out that KKC can not be applicable. Erring on caution, where credit of KKC paid is available to service provider, KKC could also be required to be paid in such cases.

## **Conclusion**

The service providers may need to ensure that bills in respect of the completed services and advance receipts is raised and service tax is paid in next month/ month next to quarter. This would ensure that there are no demands for differential service tax, citing introduction of Krishi Kalyan Cess to take effect from 1.6.2016. The customer may also not have any objection especially those who are unable to avail the credit.

Representation could need to be done to ensure the credit of KKC paid could be available for set off against not just KKC, but also against Excise duty/ service tax payable by service provider.

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