

# Tax Review

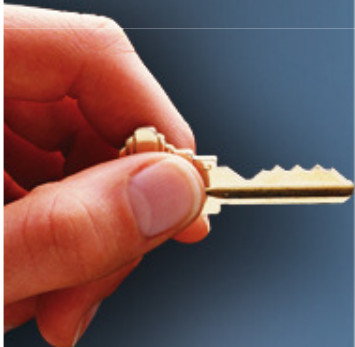
## Service Tax Update

May 2011 - Update 1

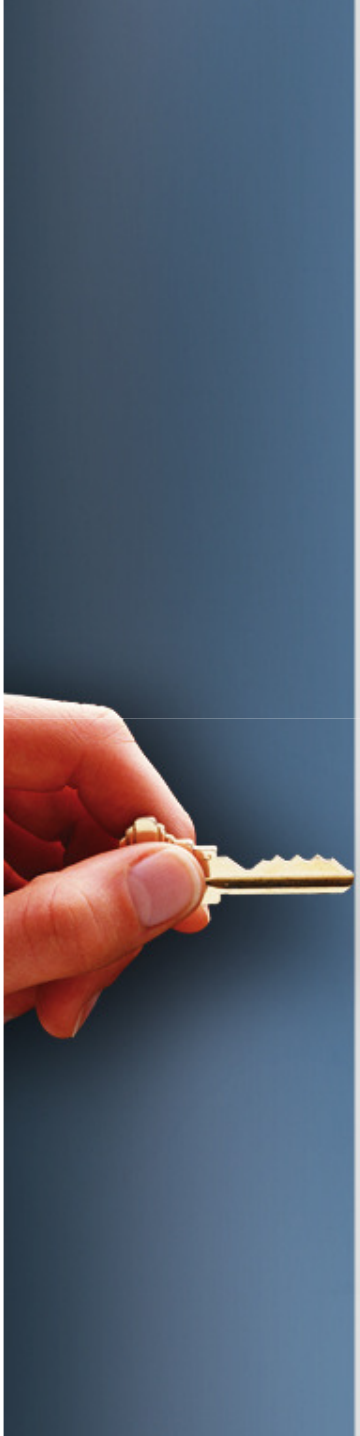


# Service Tax

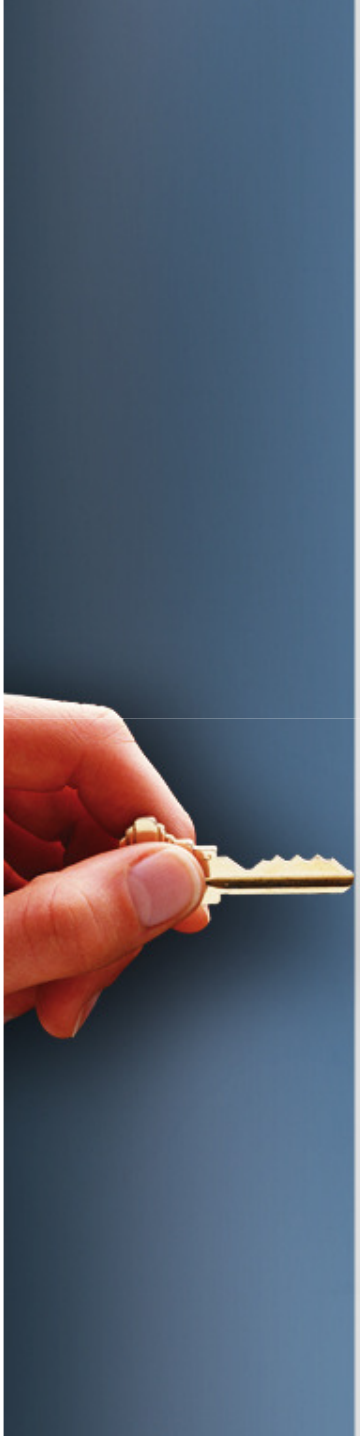
- TRU section of Department of revenue has recently issued Circular No.943/04/2011-CX dated April 29, 2011
- The Circular clarifies certain changes as made in Cenvat Credit Rules, 2004 ("Credit Rules") vide Notification 3/2011-CE (NT) dt March 1, 2011 and Notification 13/2011-CE (NT) dt March 31, 2011
- All these changes shall be effective April 1, 2011 unless provided otherwise. The following slides discuss the clarifications as issued vide this circular.



Issue	Clarification	Comments
Can credit of capital goods be availed of when used in manufacture of dutiable goods on which benefit under Notification 1/2011- CE is availed or in provision of a service whose part of value is exempted on the condition that no credit of inputs and input services is taken?	As per Rule 6(4) no credit can be availed on capital goods used exclusively in manufacture of exempted goods or in providing exempted service. Goods in respect of which the benefit of an exemption under notification No. 1/2011-CE, dated the 1st March, 2011 is availed are exempted goods [Rule 2(d)]. Taxable services whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken, are exempted services [Rule 2(e)]. Hence credit of capital goods used exclusively in manufacture of such goods or in providing such service is not allowed.	<p>Earlier Cenvat Credit on Capital goods was available on services where partial value was exempted.</p> <p>Definition of exempted goods have been expanded to include: <u>In case of exempted goods:</u> goods in respect of which the benefit of an exemption under Notification No. 1/2011-CE, dated the 1st March, 2011 is availed; <u>In case of exempted goods:</u> Services whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such services</p> <p>The restriction has increased due to expansion of definition of exempted goods and exempted services.</p>



Issue	Clarification	Comments
<p>Is the credit of only specified goods and services listed in the definition of inputs and input services not allowed such as goods used in a club, outdoor catering etc, or is the list only illustrative?</p>	<p>The list is only illustrative. The principle is that cenvat credit is not allowed when any goods and services are used primarily for personal use or consumption of employees.</p>	<p>The position taken by the department is restrictive and can cause loss of available Cenvat credit , more so in industries where assets are people like software, consulting etc. The list of services availed exclusively for personal use or consumption of employees shall lead to possible litigation. This is for the simple reason that the employer incurs such expenses as part of his business to maintain the well bring of his employees and retain them. This provides better productivity and higher revenues to the employees. Expenses such as medical insurance paid for employees, excursions, training and other likewise are clear areas where the question of personal consumption by employees may be questioned.</p>



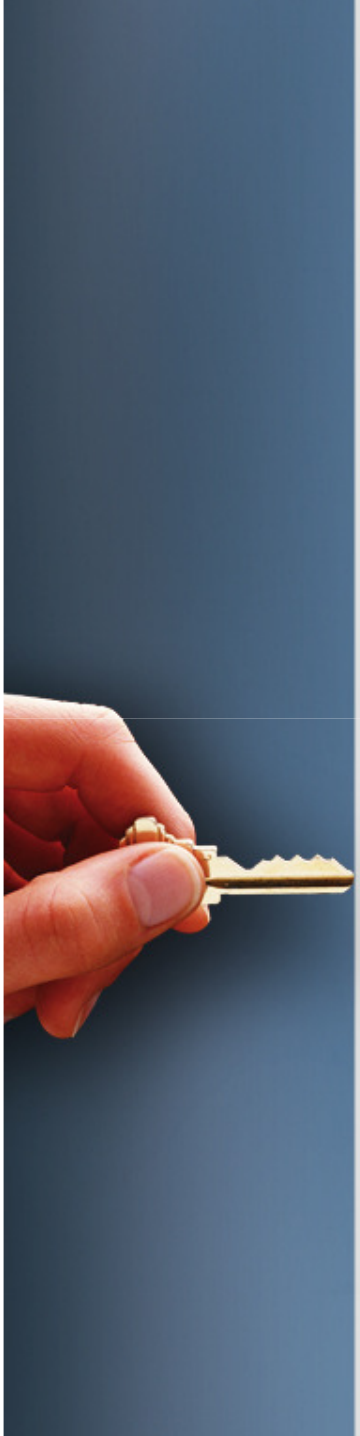
Issue	Clarification	Comments
<p>How is the “no relationship whatsoever with the manufacture of a final product” to be determined?</p>	<p>Credit of all goods used in the factory is allowed except in so far as it is specifically denied. The expression “no relationship whatsoever with the manufacture of a final product” must be interpreted and applied strictly and not loosely. The expression does not include any goods used in or in relation to the manufacture of final products whether directly or indirectly and whether contained in the final product or not. Only credit of goods used in the factory but having absolutely no relationship with the manufacture of final product is not allowed. Goods such as furniture and stationary used in an office within the factory are goods used in the factory and are used in relation to the manufacturing business and hence the credit of same is allowed.</p>	<p>This is a welcome explanation as it clarifies the understanding of a business that goods used even in office are goods used in relation to production of dutiable goods. Further, it denotes the spirit of a true value added tax.</p>



Issue	Clarification	Comments
Is the credit of input services used for repair or renovation of factory or office available?	Credit of input services used for repair or renovation of factory or office is allowed. Services used in relation to renovation or repairs of a factory, premises of provider of output service or an office relating to such factory or premises, are specifically provided for in the inclusive part of the definition of input services.	The position taken by the department is similar to the one discussed in Slide 5 above.
Is the credit of Business Auxiliary Service (BAS) on account of sales commission now disallowed after the deletion of expression “activities related to business”?	The definition of input services allows all credit on services used for clearance of final products upto the place of removal. Moreover activity of sale promotion is specifically allowed and on many occasions the remuneration for same is linked to actual sale. Reading the provisions harmoniously it is clarified that credit is admissible on the services of sale of dutiable goods on commission basis.	The clarification is a relief to assesseees and shall help in reducing litigations on this count.



Issue	Clarification	Comments
<p>Can the credit of input or input services used exclusively in trading, be availed?</p>	<p>Trading is an exempted service. Hence the credit of any inputs or input services used exclusively in trading cannot be availed.</p>	<p>This is a clear position and is alignment with Explanation II of the Rule 6(3) of Credit Rules, which provides as follows:</p> <p>Explanation II.—For removal of doubt, it is hereby clarified that the credit shall not be allowed on inputs used exclusively in or in relation to the manufacture of exempted goods or for provision of exempted services and on input services used exclusively in or in relation to the manufacture of exempted goods and their clearance upto the place of removal or for provision of exempted services.</p>



Issue	Clarification	Comments
<p>What shall be the treatment of credit of input and input services used in trading before 1.4.2008?</p>	<p>Trading is an exempted service. Hence credit of any inputs or input services used exclusively in trading cannot be availed. Credit of common inputs and input services could be availed subject to restriction of utilization of credit up to 20% of the total duty liability as provided for in extant Rules.</p>	<p>The clarification can further be interpreted to mean that such credit was available as per provisions of Rule 6 of Credit Rules post April 1, 2008 also treating Trading as exempted services. However, the Circular interprets the addition of Trading as exempted service on a retrospective basis which goes against the decision of Ahmedabad Tribunal in the case of Orion Appliances Ltd. vs. CST, wherein it was held that trading activity cannot be called a service and accordingly, this amendment as suggested may not apply retrospectively..</p>



Issue	Clarification	Comments
While calculating the value of trading what principle to follow- FIFO, LIFO or one to one correlation?	The method normally followed by the concern for its accounting purpose as per generally accepted accounting principles should be used.	No comments.
Are the taxes and year end discounts to be included in the sale price and cost of goods sold while calculating the value of trading?	Generally accepted accounting principles need to be followed in this regard. All taxes for which set off or credit is available or are refundable/ refunded may not be included. Discounts are to be included.	The clarification clearly provides that taxes which form part of Output or input Value Added Tax / Central Sales Tax may be excluded, while discounts which go to reduce the sale price / cost of goods sold need to be included.
Does the expression "in or in relation" used in Rule 6 override the definition of "input" under Rule 2(k) for determining the eligibility of Cenvat credit?	The definition of "input" is given in Rule 2(k) and Rule 6 only intends to segregate the credits of inputs used towards dutiable goods and exempted goods. While applying Rule 6, the expression "in or in relation" must be read harmoniously with the definition of "inputs".	Rule 6 does not define as to what shall qualify as input and input services. Any good or service shall qualify as input or input services only when it is in relation to a dutiable good or taxable service and thus, further test under Rule 6 may not be required.



Issue	Clarification	Comments
<p>Sub-rules 3B and 3C of rule 6 apply to whole entity or independently in respect of each registration?</p>	<p>The sub-rules 6(3B) and 6(3C) impose obligation on the entities providing banking and financial services (in case of a bank and a financial institution including a non-banking financial company) or life insurance services or management of investment under ULIP service. The obligation is applicable independently in respect of each registration. When such a concern is exclusively rendering any other service from a registered premises, the said rules do not apply. In addition to BoFS and life insurance services if any other service is rendered from the same registered premises, the said rules will apply and due reversals need to be done.</p>	<p>This clarification expands the scope of Sub-rules 3B and 3C of rule 6 to whole of a registered premises and not against the specified services. The intent is flowing from the understanding that the Cenvat credit is used towards other exempted services / incomes.</p>



Issue	Clarification	Comments
<p>Is the credit available on services received before 1.4.11 on which credit is not allowed now? e.g. rent-a-cab service</p>	<p>The credit on such service shall be available if its provision had been completed before 1.4.2011.</p>	<p>The definition of Input Service has been amended w.e.f. April 1, 2011 to include certain partial exempted services within the ambit of exempted services. Accordingly, till the same did not qualified as exempted services, Cenvat credit against such services were available. This clarification is a welcome move whereby the Department has clarified that if these services have been booked prior to the date of amendment, then credit would be available against them as per old definition.</p>



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