Levy and Collection of Tax – An Analytical Relook

This article attempts to explain the key constituents of 'GST levy and collection' along with a discussion on certain critical aspects of taxation and their corresponding impact on business operations. In terms of Article 366(12A) as inserted in the Constitution vide The Constitution (101st Amendment) Act, 2016, the term "Goods and Services Tax", is defined to mean "any tax on supply of goods or services or both except taxes on the supply of the alcoholic liquor for human consumption". Provisions for levy and collection of CGST are contained under Section 9 (Chapter III) of the CGST Act, 2017 for intra-state supply. Similar provisions are prescribed under Section 7 of the UTGST Act, 2017 for levy & collection of UTGST and in the respective States GST Act, 2017 vide Section 9 thereunder for levy & collection of SGST. Further, Section 5 of the IGST Act, 2017, governs levy and collection of IGST in case of inter-State supply. Read on…

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Constituents of GST levy

Taxable Event in GST	• GST is a tax leviable on 'supply' of goods or services or both except the supply of alcoholic liquor for human consumption. • On five petroleum products viz., petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel, GST shall be levied with effect from such date as may be notified.

Liability to pay GST	• Forward charge – Generally, the liability to pay tax in a GST regime is upon the supplier of goods or services (taxable person) in terms of Section 9(1) of the CGST Act. • Reverse charge - There are certain transactions mentioned in Section 9(3) [for specified goods/ services like GTA, Import of Services, Legal Services, etc.] and 9(4) (Exempted till September 2019) - [Procurements from unregistered suppliers of taxable goods or services or both] of the CGST Act, where the liability to pay GST is upon the receiver of such goods and / or services under reverse charge mechanism. • Specified E-com operator of services – As per Section 9(5) of the CGST Act, there are specified categories of services on which e-com operators are liable to pay tax when supplied through them like Ola, Oyo rooms etc.
Rate of tax	• Rate of tax, not exceeding 20%, as notified by the Government on recommendation of the GST Council, shall be applicable. • Different notifications are issued for rate of tax as applicable on specified goods and services.
Value of supply	• Tax shall be levied on value determined under Section 15 of the CGST Act.

I. Taxability of Employees' recovery :

'Supply' is the most critical and pivotal term under the GST regime. It is the fulcrum around which one determines the levy & collection of GST. Despite it being the taxable event, definition of supply under Section 7 of the CGST Act is a subjective and an inclusive definition, entailing wide ramifications as regards its scope.

Extending the arms of taxability, scope of supply further covers employer-employees transactions in its ambit even when there is no consideration. Para 2 of Schedule I to the CGST Act treats the following as supply:

"Supply of goods or services or both ***between related persons*** *or between distinct persons as specified in Section 25, when made in the course or furtherance of business:*

Provided that gifts not exceeding fifty thousand rupees in value in a financial year by an employer to an employee shall not be treated as supply of goods or services or both."

Note: In terms of clause (iii) to explanation (a) of Section 15 of the CGST Act, employer and employee are deemed as related persons in a GST regime.

Over the past few years, organizations have developed various ways and means, of rewarding their employees which may not necessarily be in the form of salary or bonus but may take the form of perquisites or some other benefits. While, Schedule III to the CGST Act only excludes supply of services by an employee to the employer in the course of or in relation to his employment, but, in the light of Para 2 of Schedule I, the supply of goods or services flowing from employer to employee requires due consideration of their taxability in GST either made without or with consideration.

Let us examine taxability of two most critical employer to employee transactions in GST:

- **Subsidised meals/canteen services to employees:**

As per the provisions of various enactments for instance, The Factories Act, 1948, an employer is bound to provide canteen facility to the employees. In compliance thereof, a number of companies provide meal/ canteen services to employees in factory. While some of the employers provide free food, there are certain employers providing subsidised food (a reasonable or subsidized charge is taken towards the cost of food, its preparation, and service) to the employees in their canteens and a monthly charge is deducted from their salary towards the same.

In the absence of any specific exemption in GST (as was prevalent in the service tax era under entry no. 19 and 19A of the Mega Exemption Notification No. 25/2012-ST dated 20-06-2012), the issue of taxability cropped up in the GST regime and the matter was placed before the Authority for Advance Ruling – Kerala in the application filed by ***M/s Caltech Polymers Pvt. Ltd.*** The AAR *vide* ***Order No. CT/531/18-C3 dated 26-03-2018,*** **which** ruled that the supply of food in the canteen of employer is in the course of business and the amount recovered towards supply of food is the consideration. Hence GST is chargeable on recovery of food expenses from the employees for the canteen services.

Whether the Employer Can Avail Input Tax Credit ("ITC")?

Further to the concept of taxability, is the question of availing corresponding ITC. In terms of sub-clause (i) to Section 17(5)(b) of the CGST Act, ITC shall not be available in respect of supply of outdoor catering services except where an inward supply of such services is used by a registered person for making an outward taxable supply of the same category of services or as an element of a taxable composite or mixed supply. Thus, on one hand the employer will pay GST on canteen services provided to employees at subsidized rates, but, on the other hand, it shall not be eligible to avail ITC of GST paid to the caterer managing the canteen as the employer is not in same line of business. Otherwise, also if the employer opts to pay concessional rate of 5% GST, even then no corresponding credit is allowed to him.

It is worthwhile to note that recently vide ***Notification No. 13/2018 – Central tax (Rate) dated 26th July 2018*** (w.e.f. 27th July 2018), entry no. 7(v) of *Notification No. 11/2017 - Central tax (Rate) dated 28th June 2017* dealing with applicable rate of GST on outdoor catering services has been substituted to cover *"supply, by way of or as part of any service, of goods, being food or any other article for human consumption or any drink, at Exhibition Halls, Events, Conferences, Marriage Halls and other outdoor or indoor functions that are event based and occasional in nature"*. Further, *vide* insertion of explanation 1 in entry no. 7(i), it is made explicit that supply at a canteen, mess, cafeteria or dining space of an institution such as a school, college, hospital, industrial unit, office, by such institution or by any other person based on a contractual arrangement with such institution for such supply, provided that such supply is not event based or occasional, shall attract 5% GST without ITC.

Apparently, the reference of outdoor catering services is removed from the rate notification, then denial of credit on the same renders Section 17(5)(b)(i) futile to that extent.

Further, as per one of the 46 amendments as proposed in the GST Law by the GST Council (**"draft amendments"**), it is proposed that ITC in respect of food and beverages shall be made available where the provision of such goods or services is obligatory for an employer to provide to its employees under any law for time being in force. Thus, with amendments getting approved, employers may be able to avail ITC on caterer services if GST at full rate is being charged (credit is not available where 5% GST rate is charged).

• Gifts to employees :

✓ *Gifts in the form of cash* – 'Money' is neither goods or services. Thus, gifts given in the form of cash shall fall outside the ambit of 'supply' and hence no GST implication would entail.

✓ *Non-cash gifts forming part of employment contract* – If as per the employment contract, the employees are entitled to a gift from company for a value fixed annually, then in such a situation, the employer is under an obligation to provide gifts based on the terms mentioned in the employment contract and as such these gifts will not partake the character of 'gift' as discussed in para 2 of schedule I.

Such gift is a consideration for the services rendered by the employee in the course of employment and hence not liable to GST based on para 1 of schedule III i.e. treated as a part of CTC (refer press release dated 10th July, 2017).

✓ *Non-cash gifts provided otherwise & not forming part of employment contract* - If the company offers gifts to employees voluntarily may be on some occasion or festival which does not form part of employment contract/CTC, and the value of such gifts exceeds ₹ 50,000/- in value in a financial year, then the same shall be treated as supplies to employees without consideration and attract GST.

Whether the employer can avail ITC?

Having understood taxability of gifts in the hands of employer, subsequent question which arises is determination of eligibility to avail credit of GST paid on procurement of such gifts. The answer to this also is not affirmative as clause (h) of Section 17(5) of the CGST Act, specifically restricts ITC on *"goods lost, stolen, destroyed, written off or disposed of by way of gift or free samples"*. This gives an impression of double taxation on all gifts which get covered under para 2 of schedule I. Ideally, the law must be amended so as to allow ITC on gifts when appropriate GST has been paid on its disposal. Alternatively, refusal to take credit on gifts should suffice the requirement to pay tax under para 2 of schedule I.

II. Tolerating an Act: A Supply with no Supply!!

Para 5(e) of Schedule II to the CGST Act, intends to cover agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act, as supply of services in GST. Manifestly, as per Para 5(e) of Schedule II, the scope of levy of GST would apply to even a situation where the actual activity is non-existent, consequently a person would be required to pay tax even for not doing anything. Even if a person refrains from doing a particular activity for which a consideration is received or receivable, such consideration would be taxed. Further, definition of the term 'consideration' under Section 2(31) of the CGST Act also includes the monetary value of any act or forbearance; in respect of, in response to, or for the inducement of, the supply of goods/ services, whether by the recipient or by any other person.

The foregoing inclusion in the term "supply" has substantially enlarged the scope of GST to a great extent and issues of taxability are arising in following cases:

- **Notice pay recovery:** While salary in lieu of notice period paid by employer to employee will fall outside the scope of GST in terms of para 1 of schedule III i.e. services by an employee to the employer in the course of or in relation to his employment, but taxability of notice pay recovery made by an employer from employee has been a contentious issue since service tax era. Tax collectors may demand GST on notice pay recovery from the employee, contending the same as consideration for tolerating an act, more so because in GST the definition of consideration itself has been expanded to include the monetary value of any act or forbearance. Hence, taxability of notice pay recovery from employee as on date contentious and vexed issue.
- **Liquidated damages (LD): The matter of taxability of liquidated damages under GST as supply of services was placed before the** Authority for Advance Ruling – Mumbai in the application filed by ***M/s Maharashtra State Power Generation Company*** *Limited.* The AAR *vide* ***Order No. GST-ARA-15/2017-18/B-30 Mumbai dated 08-05-2018***, and after perusal of agreements ruled that GST would be applicable on LD amount charged by the company. After perusing the contract and related documents, Ld. AAR found that the contract price and the liquidated damages are two different aspects and noted that deduction of amount as payable to the contractor is a mere facilitation towards the adjustment of the accounts. Thus, it was observed that the levy of LD was specifically identified as an independent levy under the contract and hence taxable.

Conflicting view point: It may be argued to say that a contract is basically entered into for performance and not for its breach and hence such an activity done without a relationship i.e. without the express or implied contractual reciprocity can't be argued to be performed for a consideration within the meaning of the Indian Contract Act.

Further, Para 5(e) of Schedule II is intended to tax arrangements where the primary intention is to tolerate an act or situation which is clearly distinguishable from the above situation in hand. But, this shall be a subjective issue prone to litigation.

Proposed amendment – **In the draft amendments,** the term 'supply' is proposed to be amended to exclude activities/ transactions listed in Schedule II to ensure that the activities/ transactions as per Schedule II is to decide only whether the same is supply of goods or services. Hence, activities/ transactions listed in Schedule II (as supply of service or supply of goods) shall be taxed only when they constitute 'supply' in accordance with provisions of Section 7(1)(a), (b) and (c) of the CGST Act. With this change in definition of 'supply', above issues of taxing non-virtual activities which absent supplies may come to rest.

III. Taxability of Services Provided by One Unit to Other Unit of Same Company

In terms of Para 2 of Schedule I to the CGST Act, supply of goods or services or both between related persons or between distinct persons as specified in Section 25, when made in the course or furtherance of business, is chargeable to GST even if no consideration is flowing between them. Definition of related persons given under Explanation to Section 15 of the CGST Act is wide enough to cover two persons wherein one directly or indirectly controls the other and also if both these persons are directly or indirectly controlled by a third person.

Further, 'place of business' in GST includes every place from where the business is carried on. Thus, the entities having operations from more than one state will have to obtain separate registration in each such state where from they are supplying goods or services i.e. they are operating. Each operating location in different states or same state if separate registration is taken, will be treated as distinct persons [Section 25] and transactions between the two distinct persons, whether with consideration or without consideration, will be liable to GST.

In the context of supply of goods, the scenario may not create an issue as physical movement of goods between different units/branches of a company is easily traceable. As far as supply of services are concerned, in erstwhile service tax regime, tax was levied only when services were rendered by a person to another for consideration [subject to exceptions that:

(i) an establishment of a person located in taxable territory & another establishment of such person located in non-taxable territory; and

(ii) an unincorporated association/body of persons and a member thereof, would be treated as distinct persons].

In GST, even supply of services within the company, say head office providing services to branch office or vice versa, will be covered under the taxable net as Para 2 of Schedule I is applicable on supply of such services even without consideration. It is in the light of above that it becomes important for any business entity to identify all the transactions between their distinct entities, which may or may not be apparently identifiable.

The Hon'ble Authority for Advance Ruling, Karnataka while deciding the application filed by ***M/s Columbia Asia Hospitals Private Limited [Advance Ruling No. KAR ADRG 15/2018 dated 27th July 2018]***, has ruled that the activities performed by the employees at the corporate office in the course of or in relation to employment such as accounting, other administrative and IT system maintenance for the units located in the other states as well i.e. distinct persons as per Section 25(4) of the CGST Act shall be treated as supply as per Para 2 of Schedule I of the CGST Act. Further, the valuation includes all costs, the employee cost also needs to be taken into consideration at the time of valuation of goods or services provided by one distinct entity to the other distinct entities.

This ruling is going to have outspread ramifications if suitable clarification as to exact scope of Para 2 of Schedule I in respect of inter-company supply of services is not clarified immediately. Undoubtedly, any inter-company supply of goods or services is under the taxable net of GST but extending the same to even cover employees' cost will create chaos in multi-state operational companies. It is not just practically impossible to track all such employees' cost but shall also burden companies with enhanced compliance procedures. Situation will worsen if the other recipient unit of the Company turns out to be engaged in supply of exempted goods or services, as they will not be entitled to avail credit of GST charged by supplier unit of their Company. Ideally, there should not be any taxability on employees cost in terms of Para I of Schedule III i.e. services by an employee to the employer in the course of or in relation to his employment treated neither as supply of goods nor services.

IV. Actual Recipient Vs. Deemed Recipient: Taxability of Ocean Freight in Case of Import of Goods on CIF Basis

In terms of S. No. 10 of ***Notification No. 10/2017 – IGST (Rate) dated 28th June 2017***, services supplied by a person located in non-taxable territory by way of transportation of goods by a vessel from a place outside India up to the customs station of clearance in India, taxable under reverse charge. Further, the Notification also mentions that in such case, importer, as defined in Section 2(26) of the Customs Act, 1962, located in the taxable territory, shall be the person liable to GST under reverse charge i.e. as per the Notification, importer is considered as the deemed recipient of the services.

But, drawing reference from definition of 'recipient' under Section 2(93) of the CGST Act, would reveal that as per clause (a) ibid, where consideration is payable for supply of goods or services, then the person liable to pay consideration shall be considered as the 'recipient; of supply of goods or services. Meaning thereby, the exporter shall be considered as the recipient of services in case of CIF contracts. This creates an anomaly as to the concept of deemed recipient under Notification 10 viz-a-viz actual recipient as per the definition of 'recipient' under GST Laws and also doubts the legal sanctity of IGST levy on importers as per Notification 10.

This aspect was challenged before the Hon'ble Gujarat High Court (HC) in ***Mohit Minerals Pvt. Ltd. Vs. Union of India [2018-TIOL-06-HC-AHM-GST]***, wherein interim relief was granted to the petitioner. But, the Hon'ble AAR, Uttarakhand in an application filed by ***M/s Bahl Paper Mill Ltd.***, held that even if importer has paid IGST on CIF value of imported goods, still IGST on ocean freight is payable. Mere filing of application before the HC does not render notification ultra vires until the same is turned down.

Our Comments:

GST, which was implemented by the Government from 1st July 2017, is without doubt the most significant and pathbreaking economic reform in the country since Independence. Despite of being mocked by opposition, GST–the India's new unified nationwide value-added system of taxation has come a long way in simplifying the complex tax structure of the Country. Initial anxieties are settling to an extent with the passage of time, but still there is long way for GST to eventually be called a 'Good and Simple Tax' in real sense. As GST's first anniversary passes, the Government is expected to tweak the tax regime through draft amendments during the ongoing monsoon session of Parliament in July. Though lots of worries of the Industries have been addressed with proposed amendments in GST Law which is indeed heartening for taxpayers, but still there are many other open areas lacking clarification which also requires to be addressed appropriately. ■

Don't get so busy making a living that you forget to make a life — Dolly Parton