



Construction and Real Estate

Impact of Model GST Law

How did it all start ?



No VAT on Works Contract

Deeming Provisions introduced in Constitution

Theory of Dominant Intention

Splittable and Non-Splittable Composite Contracts

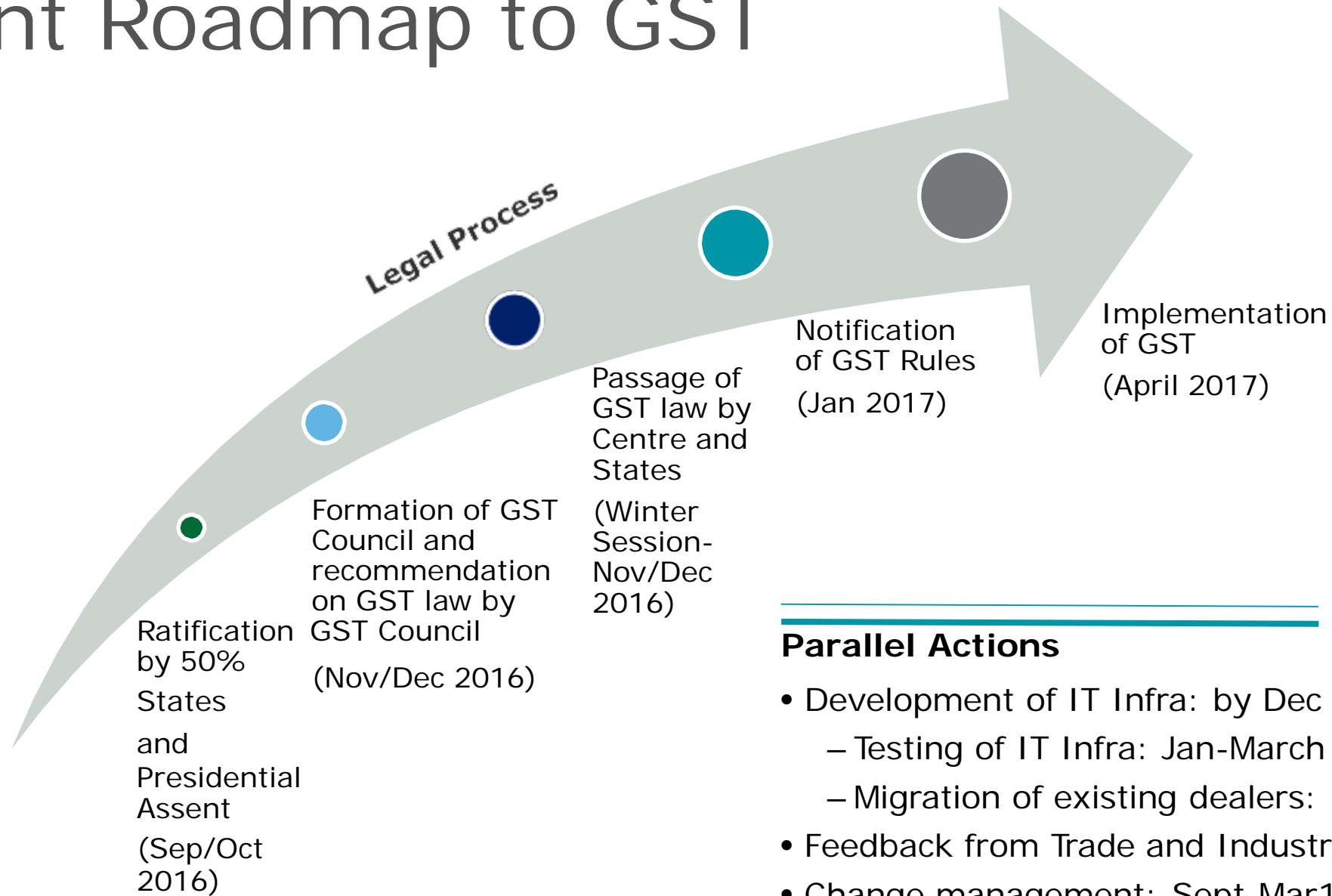
Builder vs Developer

Introduction of Service tax on builders

Developer is also a Works Contractor

Overlapping of Goods, Service and Land while calculating taxes

Current Roadmap to GST



Parallel Actions

- Development of IT Infra: by Dec 16
 - Testing of IT Infra: Jan-March 17
 - Migration of existing dealers: Feb-Mar 17
- Feedback from Trade and Industry: Aug- Oct 16
- Change management: Sept-Mar17

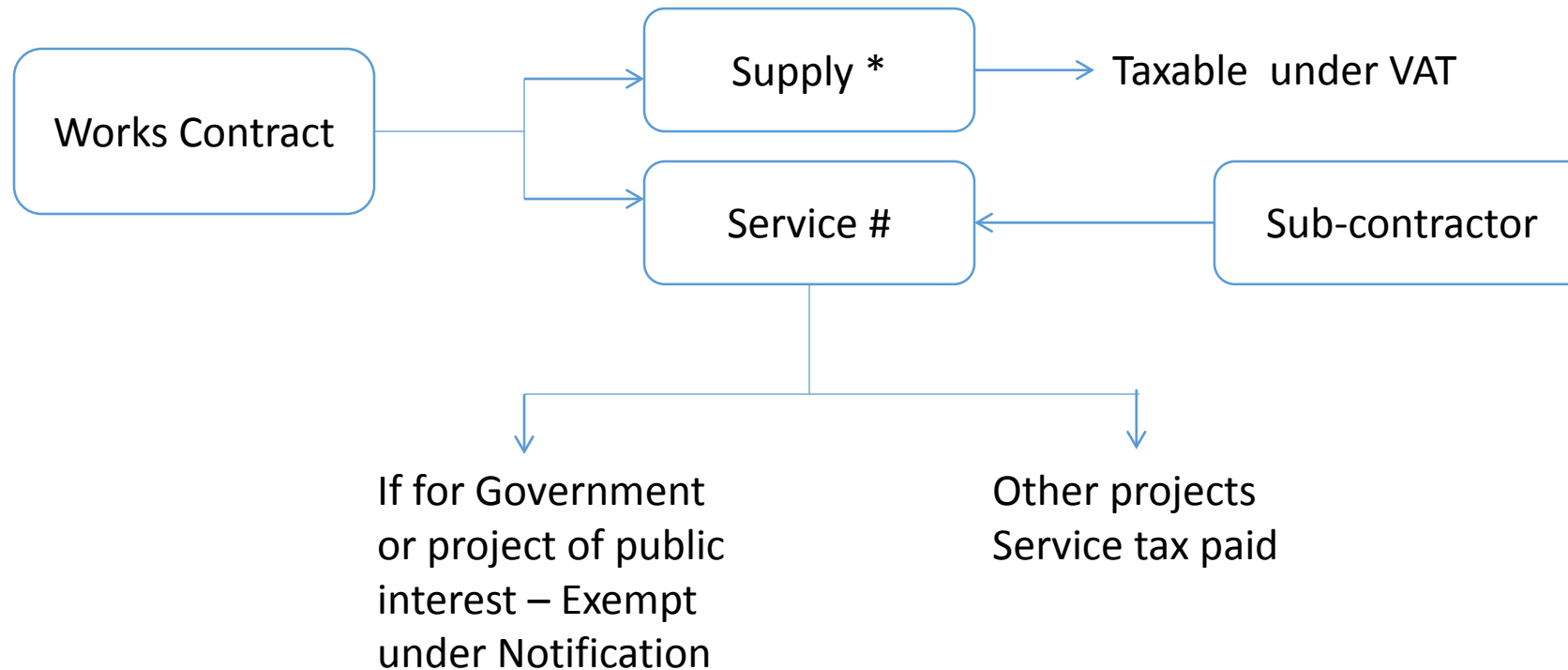
Taxes to be subsumed in GST



Note:

- 1) Alcoholic beverages for human consumption are proposed to be kept out of the purview of GST
- 2) GST on petroleum products would be levied from a notified date recommended by the GST Council
- 3) * Includes Excise duty levied under Medicinal & Toilet Preparations (Excise Duties) Act, 1955

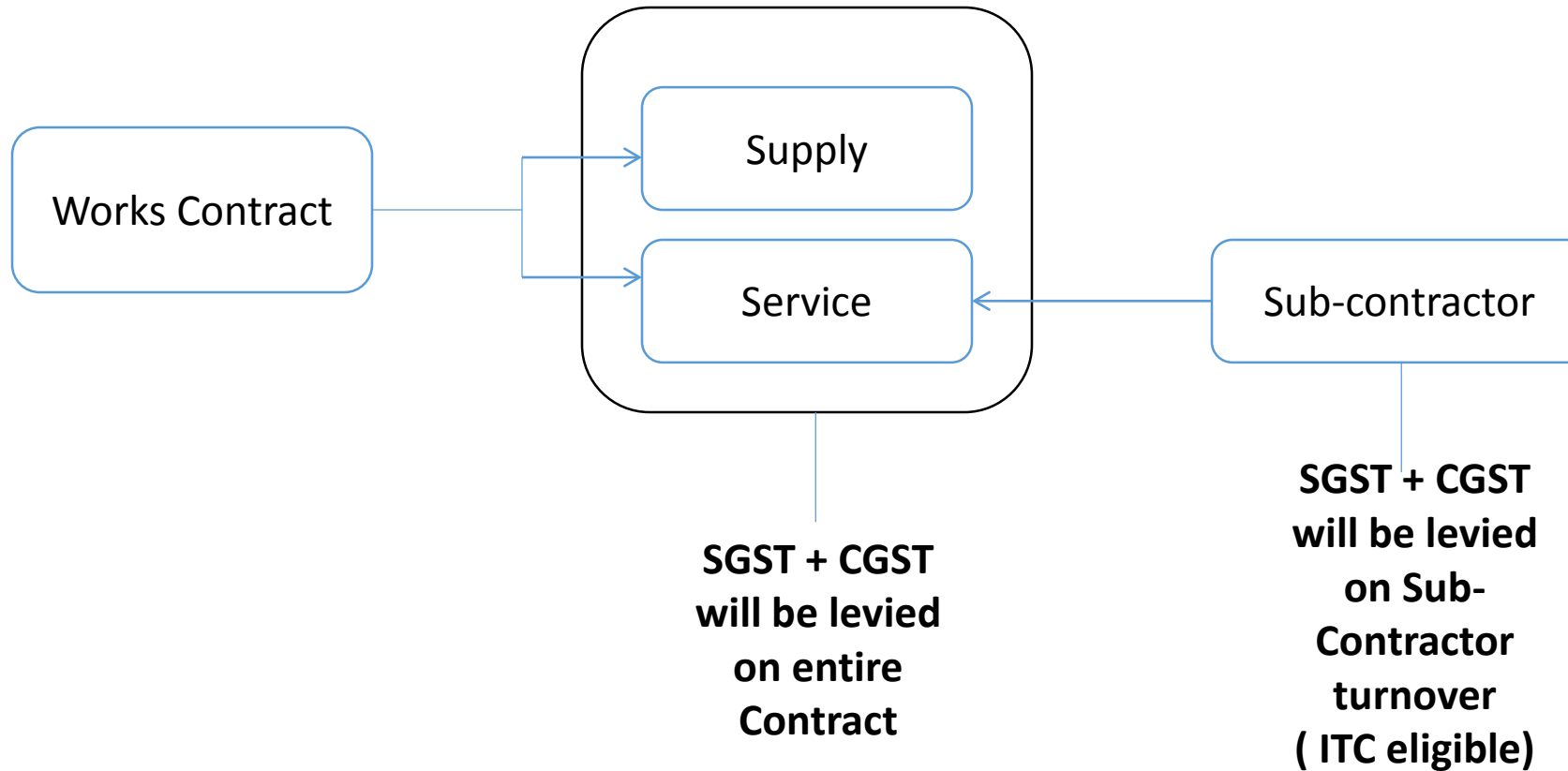
Works Contract under present regime :



* VAT turnover assessed under VAT Act, after allowing deduction for labor, Interstate supply, Supply in the course of Import etc. Often results in litigation

Service tax exemptions are often disallowed; also claim for abatement is disputed on different grounds –Original Works etc. ?

Works Contract under GST regime :



Input tax credit on SGST+ CGST or IGST paid on is available. Input tax credit on SGST + CGST paid by Sub-contractor is available.

Service means “anything other than goods” – so Works Contracts is covered under this category – which may attract full GST unless – a separate lower rate is fixed for Services

GST impact on Construction

Sector

Developer / Contractor

Output Service

Procurements

Input Services

Inputs / Capital goods

Service tax + VAT

- Present regime – rate is 15%*30% + 0.6%
- GST regime - rate in the range of 18%- 20%

Service tax (Domestic / Imports)

- Present regime – Creditable
- GST regime – Creditable

Imports

Domestic

CVD

- Present regime – Creditable
- GST regime – Creditable

SAD

- Present regime – not Creditable
- GST regime – Creditable

Excise duty

- Present regime – Creditable if procured from manufacturer / dealer
- GST regime – Creditable

VAT / CST

- Present regime – not Creditable
- GST regime – Creditable

Impact - Negative

Impact - Neutral

Impact - Neutral

Impact - Positive

Impact - Positive

Impact - Positive

Draft GST Law, 2016

- Salient Features :

- Model CGST Law and SGST Law to be put in place along with Rules
- Separate IGST Law for each state and single CGST and IGST Law across the country
- Customs on Import shall continue
- Extend to whole of India including J&K
- Changes in the SGST Law can be done based on recommendation of the GST Council
- Some flexibility to states in terms of rules and band of rates
- Uniform IT Platform expected
- Each Transaction to be subjected to either CGST + SGST or IGST
- Critical Points on which consensus is pending to be built :-
 - GST Rates
 - Exemption Threshold
 - Composition Scheme Threshold
 - Exemption / Negative List

Relevant Definitions



(48) “goods” means **every kind of movable property** other than actionable claim and money but includes securities, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before supply or under the contract of supply;

(88) “services” means **anything other than goods**;

Is Classification between goods and services still relevant ?

Splitting of Contract –

Whether relevant under GST??

Relevant Definitions



(88) “services” means **anything other than goods**;

Why such a wide definition of service ?

- ✓ **Definition of “services”** – very extensive (**Risky**). Explanation added is not a part of definition as given in proposed Article 366(29A) of Constitution.
- ✓ Whether the services includes immovable properties as the same is not included in the “goods” ?

Exchange - JD



The definition of service under GST **includes actionable claim and supply** of same with or without consideration.

Whether **Transferable Development Rights (TDR)** would be taxable under GST ?

Relevant Definitions



(107) “works contract” means an agreement for carrying out

- for cash, deferred payment or other valuable consideration,
- building, construction, fabrication, erection, installation, fitting out, improvement, modification, repair, renovation or commissioning.
- of any movable or immovable property;

Works Contract

Definition of “works contract”

- No condition of transfer of property in goods
- does not contain "any other similar activity" like the Finance Act 1994
- **New words added** - building, fabrication (may be because fabrication leads to manufacture so it was not there earlier), improvement;
- The expression "**construction**" includes **additions, alterations, replacements or remodeling of any existing civil structure;**
- The concept of original works – **Removed.**
- The earlier leaked version talked only of immovable property, but the latest one talks of both moveable and immoveable property
- Surprisingly there is no reference of “maintenance”



Definition of “works contract”

- What about other completion services ?
- What if pure labour services are provided however the materials are issued by principal ?
- What about onsite manufacturing ?
- What about made to order goods ? Whether they are covered here ?



Relevant Definitions



(27) “composite supply” means a supply consisting of -

(a) two or more goods;

(b) two or more services; or

(c) a combination of goods and services provided in the course or furtherance of business, whether or not the same can be segregated;

Relevant Definitions



“composite supply”

- Is not referred to in any of the sections within the act ?
- No provisions on bundling under GST
- Relevance of the theory of dominant intention

Meaning & Scope of Supply

Supply includes :-

- all forms of supply of goods and/or services such as sale, transfer, barter, exchange, license, rental, lease or disposal
- made or agreed to be made for a consideration by a person
- in the course or furtherance of business,

Meaning & Scope of Supply

Section 3(3) of the Draft Act-

- Centre / State may upon recommendation of the Council, specify, by notification, the transactions that are to be treated as –
 - A supply of goods and not as a supply of services or
 - A supply of services and not as a supply of goods or
 - Neither a supply of goods nor a supply of services

Supply



- Schedule I – Without Consideration
 - Supply of goods and / or services by a taxable person to another taxable or non-taxable person in the course or furtherance of business –
 - Supply of Free Issue Materials ?
 - Branch Transfers from one site to another ?
 - This will impact refunds / excess Cenvat Balance

Supply



- Schedule II – Declared Services
 - Any treatment of process which is being applied to another person's goods
 - Construction of Complex
 - Works Contract including transfer of property

“Supply of Service”

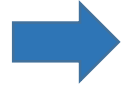


❖ **Schedule II of GST Model Law, following is the “Supply of Service”:-**

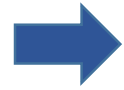
- ✓ Construction of,
 - a complex
 - building
 - civil structure or part thereof
- intend for sale to a buyer, wholly or partly **except where the**
- entire consideration has been received
- after issuance of completion certificate, where required, by the competent authority
- or
- **before its first occupation**, whichever is earlier

Whether external certification required to prove first occupation

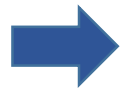
Supply



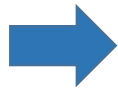
Can supply of goods in execution of Works Contract be treated as a supply ?



The constitution – Works Contract is deemed sale of goods however GST Law states it is “Supply of Service” ?



In article 366 (12A) of the Constitution - “goods and services tax” means any tax on supply of goods, or services or both



Article 366 (29A) defines ‘deemed sale of goods’ – retained under GST Law:

- o In 2011 bill this article was proposed to be deleted
- o Covers transactions of works contract, sale of food articles, transfer of right to use goods, hire purchase, etc.
- o No reason to continue this article under GST
- o May be retained on a safe side as Supply includes sale

Valuation under GST



No choices available as of now
Full value of consideration to be
treated as a service
Subject to GST at Full rate

Valuation



Determination of value of Supply of Goods & Services:-

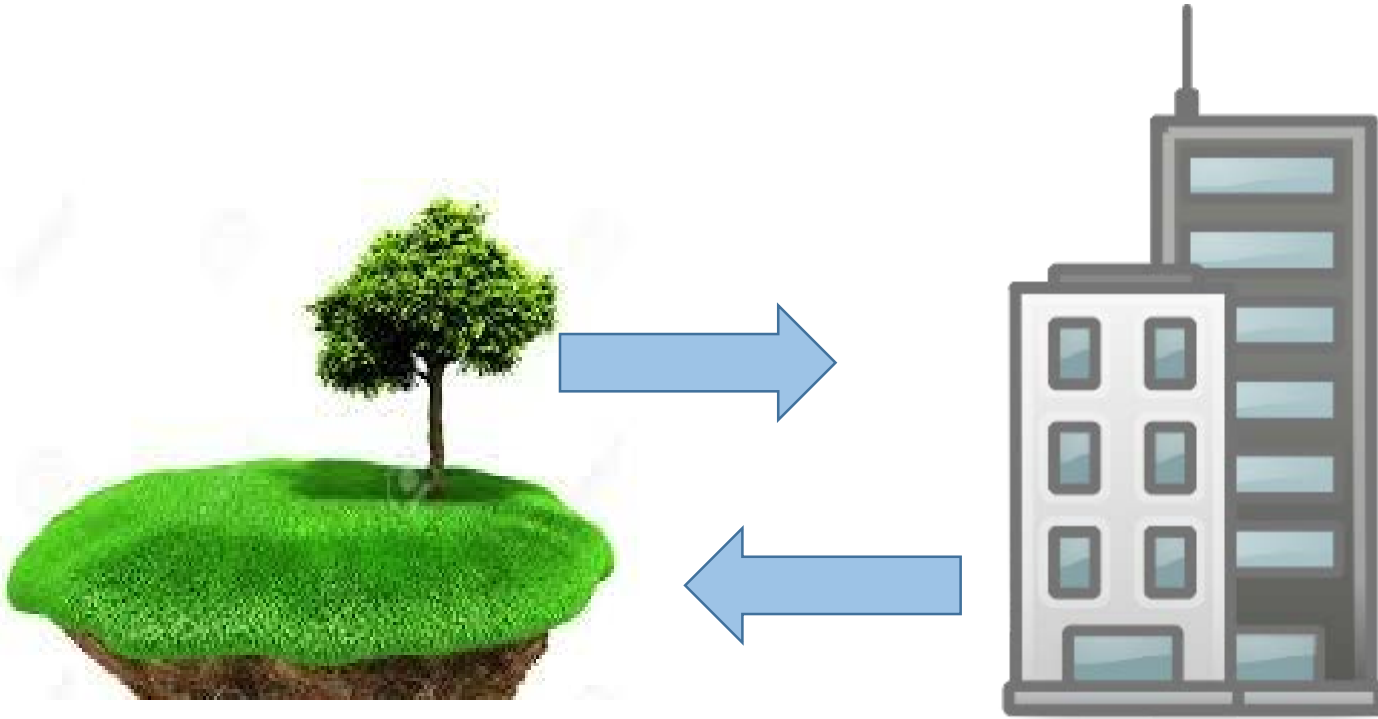
↓ “transaction value”

↓ Value by Comparison.

↓ Value shall be cost of goods / services + Charges + profit -
Computed value method

↓ The value shall be determined using reasonable means
consistent with the principles and general provisions -
Residual method

Exchange - JD



Flats / Units / Shops given free of cost in lieu of land cost

Whether GST is payable in respect of free flats / units transferred to land owner as a cost of land.



Treatment of under Constructed property



Currently as per the GST Law model GST on sale of immovable property i.e. agreement with the buyer before completion certificate is payable on entire amount.

Issue is arguable.

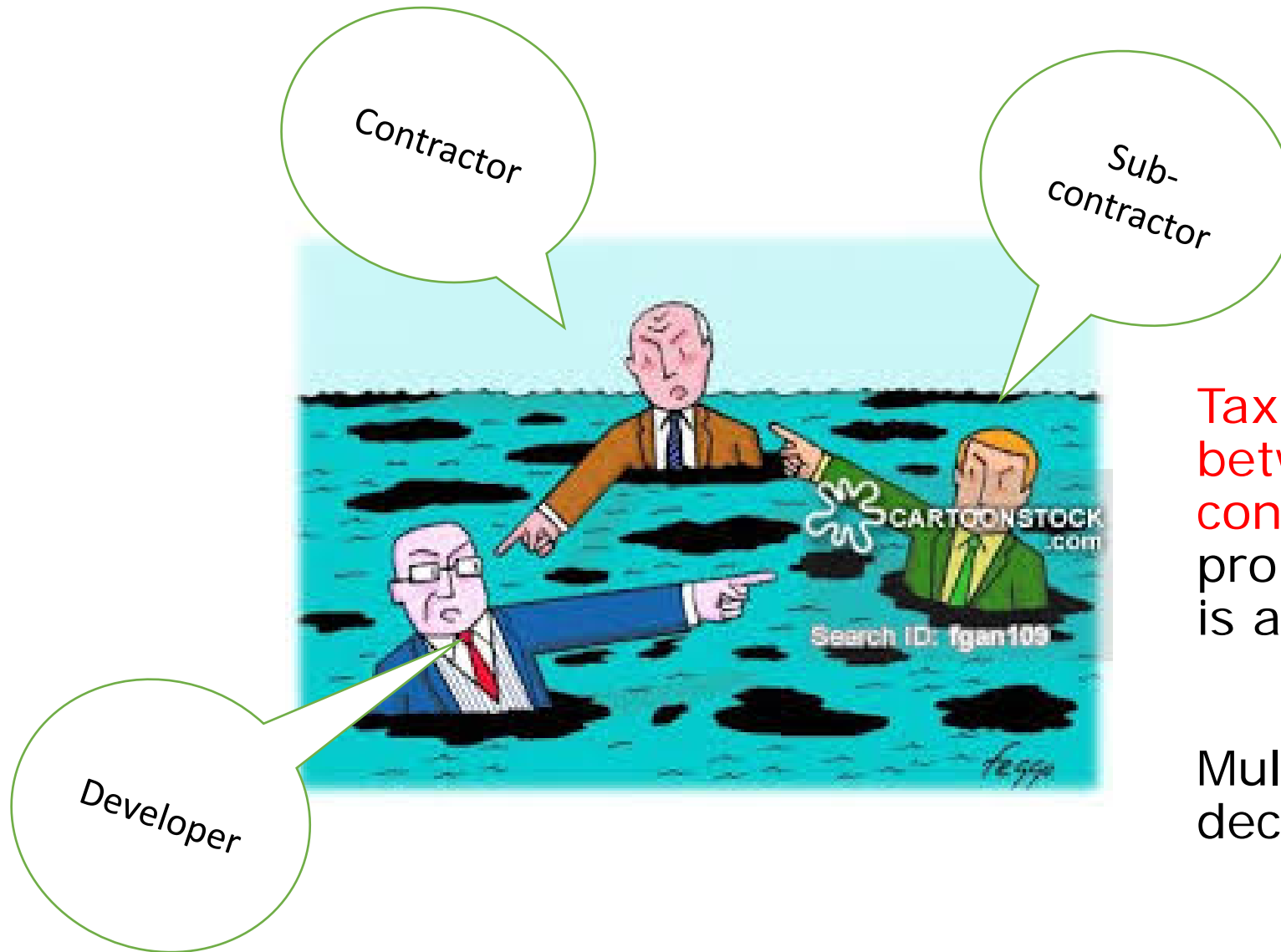
Treatment of Land



As per the tax laws prevailing in Australia and Singapore, GST is levied on transfer of land despite the same being offered to a land transfer tax, however the same is exempt from GST in United Kingdom.

It would be interesting to see which tax treatment the Indian Government will adopt.

Current draft is silent on treatment of land ?



An Open Issue under GST:-

Taxability on agreement between contractor and sub-contractor for construction of property; whether exemption is available to sub-contractor.

Multiple deemed sales were declared invalid in L&T 17 VST

GST – Negative List and Exemptions

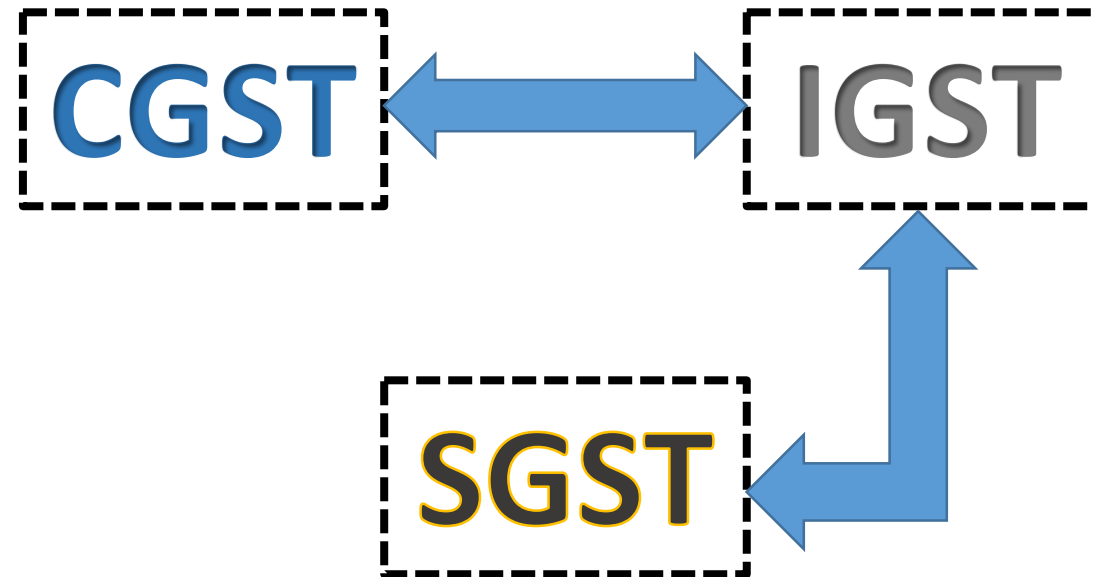


Exemptions

- Central Government has been granted to reduce GST Rates as per requirements by issuing a general exemption notification
- Exemption optional but absolute exemption compulsory
- Composition Scheme – Turnover does not exceed – Rs. 50 Lakhs
- Scheme is Optional – all supplies should be within the state
- Scheme is useful to persons who are making direct sale to consumers
- No clarity so far as far as other exemption are concerned
- No Negative list within the act



Input Tax Credit



Input Tax Credit

- What about credit reversal in case of units sold after BU / Completion certificate which are currently exempt under GST ?
- Whether input on common services or total input to be reversed ?

Input Tax Credit

Exclusions are a big blow :-

(c) goods and/or services acquired by the principal in the execution of works contract when such contract results in construction of immovable property, other than plant and machinery;

(d) goods acquired by a principal, the property in which is not transferred (whether as goods or in some other form) to any other person, which are used in the construction of immovable property, other than plant and machinery;

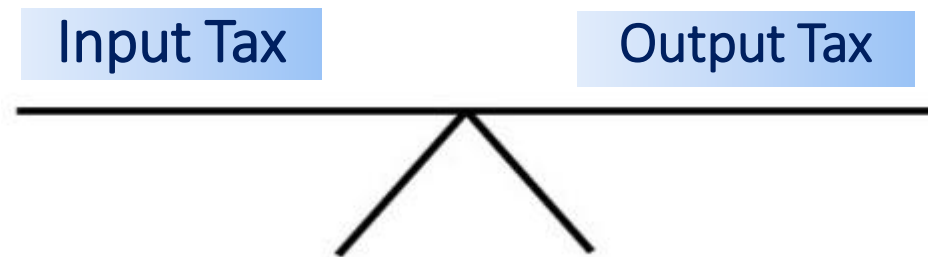
- Pure services not resulting in works contract seem to be missing



Input Tax Credit



- Not clear why the term 'Principal' is used – Whether this would also include main contractor or the developer ?



TDS / Reverse Charge Mechanism

Reverse Charge Mechanism

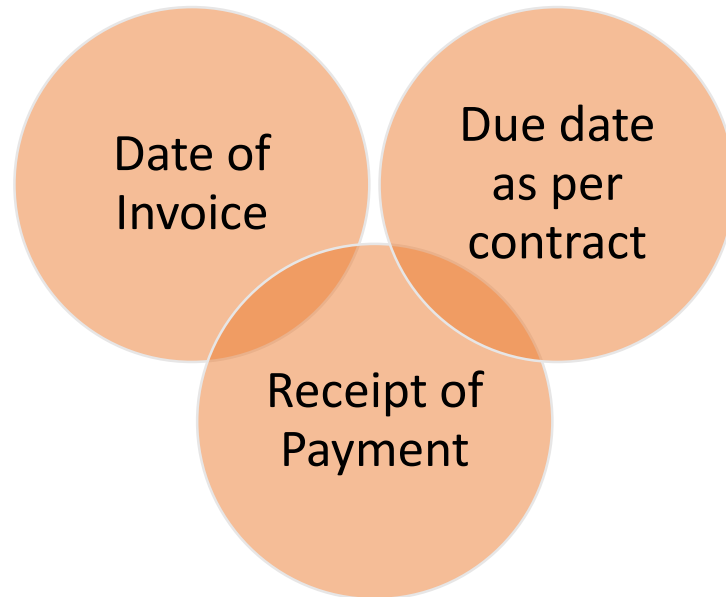
- Aggregate Turnover – does not include supplies applicable under RCM
- Output tax – excludes tax payable on RCM (excluded to restrict input tax credit)
- Person required to be registered irrespective of threshold limit
- No specific provisions indicating specific reverse charge shall be applicable – may specify through Rules

TDS

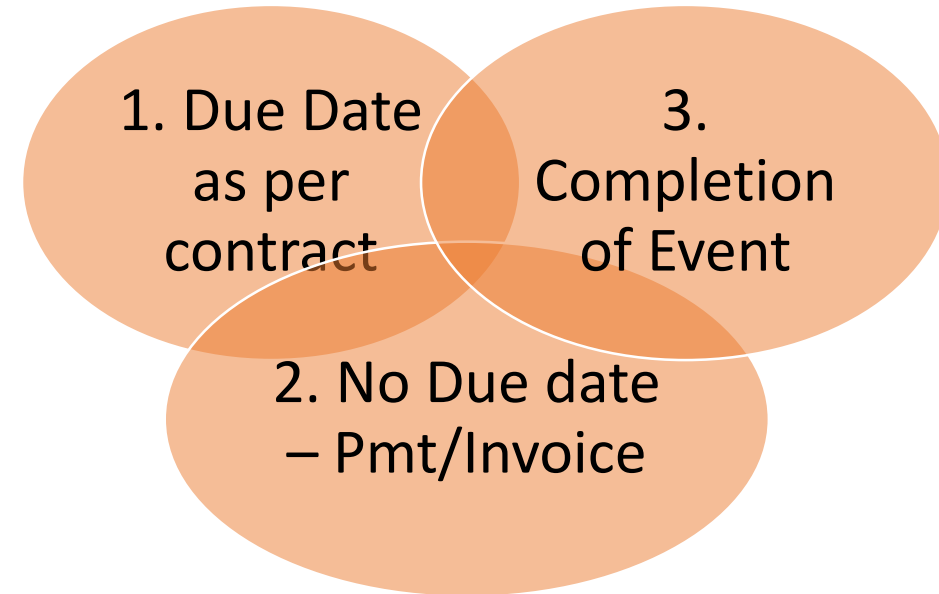
- Applicability:
 - Department of Central & State Government
 - Local Authority
 - Government Agencies
 - any other 'persons' as may be notified
- Rate of TDS – 1%
- Certificate of TDS by Deductor to Deductee
- Deductor – to file electronic return
- Credit of TDS available to deductee in electronic cash ledger

Identifying the date on which tax is due – Time of Continuous Supply of Services

Currently



Under GST



Critical Issues expected to be faced :-

- a. Advisable not to document due dates in the contract
- b. Completion of Event clause to be properly drafted
- c. Advisable to be based on certification of work

Identifying the state in which tax is due - Place of Supply (Current Regime)



- No such concept under Central Excise / State VAT
- Concept of Place of provision of Service (POPS) in service tax to decide import / export
 - The residual or general principle is that the location of recipient of service is place of provision of service
 - Whereas separate rules have been prescribed for separate services wherein different places of provision of service are defined
- Under CST, the principles determining situs of sale is prescribed in Chapter II of Central Sales Tax Act, 1956
 - The major principle for determining situs of sale is the location of sale that occurs on the movement of goods





-: Relevant Definitions :-

- (64) “**location of recipient of service**”
- (i) **place of business**;
- (ii) **fixed establishment**;
- (iii) Multiple **establishment most directly concerned** with the receipt
- (iv) in absence of such places, **usual place of residence of the recipient**;



(65) “**location of supplier of service**”

Where the supply is made from

- (i) **place of business** ;
- (ii) **fixed establishment**;
- (iii) **establishment most directly concerned** with the provision of the supply;
- (iv) in absence of such places, the **usual place of residence of the supplier**;

Meaning of “Supply is made” ?

In a construction project supply is always received at the construction site as per POS, but can we say that supply is also made at the construction site so as to require local registration ?

- Whether a Real Estate developer having Head office at Gujarat and Project Site at Maharashtra would be required to obtain registration under SGST for both locations or it would be ok if he pays IGST
- While paying IGST do we have to select account code of IGST or IGST – Maharashtra ? Its relevance and what if there is a mistake ?
- **Whether the site at Maharashtra is a :-**
 - Place of Business
 - Principal Place of Business
 - Fixed Establishment
 - Place of residence
- What if all goods are directly billed from Gujarat to the buyers at Maharashtra ?

Place of Supply-Services

Supply of services to registered person

- Location of recipient of service

Supply of services to other than registered person

- The location of the recipient where the address on record exists, and - the location of the supplier of services in other cases

Construction is deemed service whether involving goods or not

- Place of Supply Rules :

- 3rd party supplies (such as bill-to/ ship-to or sale in transit):
 - ✓ Section 5(2A) of the Model IGST Law states that where the goods are delivered on the direction of a third person, whether as an agent or otherwise, before or during movement of goods, either by way of transfer of documents of title to the goods or otherwise, it shall be deemed that the said third person has received the goods and the place of supply of such goods shall be the principal place of business of such person.

- Place of Supply Rules :



- The place of supply of services, in relation to an immovable property, would be the location at which the immovable property is located or intended to be located.
- In case of multi state project, based on revenue collected for such place as per Contract.
- Thus Works Contract services it would be mostly the place where works contract is being executed and completed project is handed over to Customer.
- Determination of place of supply in cases of transshipment and bundling of goods before delivery undertaken – not clear and lacks clarity
- Please refer EU Regulations on this issue

Transitional Provisions



159. Treatment of long term construction / works contracts

The goods and/or services supplied on or after the appointed day in pursuance of a contract entered into prior to the appointed day shall be liable to tax under the provisions of this Act.

(CGST Law)

The goods and/or services supplied on or after the appointed day in pursuance of a contract entered into prior to the appointed day shall be liable to tax under the provisions of this Act.

Transitional Provisions – Input Tax Credit

- Eligible CENVAT Credit can be carried forward – clause 143(1)
- Eligible State VAT Credit can be carried forward – clause 143(2)
- Unavailed credit on eligible capital goods not carried forward in a return can taken – clause 144(1)
- Eligible duties and taxes exempt prior to GST and taxable in GST – credit can be availed on such inputs and inputs contained semi-finished and finished stock on date of introduction of GST on the basis of GAAP – clause 145
- Credit can be availed if the person switches from composition to normal scheme – clause 146

Transitional Provisions – Missing Points

- CST paid on goods lying in stock to be used in taxable supply in GST
- Service tax/ Excise credit for VAT dealers or vice-versa

The underlying principle is that- these goods and services would be used in the provision of output goods or services chargeable to tax under GST regime.

- There is reference of Stocks and inputs in FG and SFG, however there is no reference of Work in Progress of a developer / contractor
- Returning the FIM lying with the contractor as on the date of GST

GST Impact on Projects

- Structuring of sourcing will lose relevance
- Sale in course of import etc. will lose relevance (High Seas Sale not impacted)
- Value addition by contractor will get taxed (Sale in Course of Import, Sales in Transit under CST 6 (2), Specialized Regd. Dealer)
- Project cost to go up wherever ITC ineligible to Project Owner
- Cash flow to get impacted as tax to be paid upfront and then ITC to be taken – Branch Transfer transactions..
- Place of Supply may be linked to Project location
- Contractor to pay GST on receipt of payments/ invoicing as per milestones and take credit of input taxes

GST – Action Points



Focus Areas	Action points
Contracts extending beyond 31.03.2017	<ul style="list-style-type: none">✓ Statutory variation clause – does it covers GST related changes ?✓ Amendments – to effect changes in sourcing/ procurement etc.✓ Assessment of impact of GST provisions on each contract / project
Accounting preparedness	<ul style="list-style-type: none">✓ New GL codes/ COA – mapping within ERP/ Hyperion✓ Existing Excise/ VAT assessments may continue for few years✓ Existing Invoice system – compatibility with GST requirements✓ GST will take away flexibility – manual adjustments
Transitional issues	<ul style="list-style-type: none">✓ Existing VAT assessments – pressures to complete will increase, pending statutory forms demand ..✓ Closing CENVAT balances/ VAT ITC credits – monetization✓ Form collection drive/CENVAT audits to be carried out



Conclusion

- **Not an ideal GST** - considering the present political situation , this is the best that could be achieved.
- The proposed GST will surely be better than the existing situation.
- IGST & concept of 'supply' are the game changers. It will help in developing national market and considerably reduce the cascading effect of taxes.
- Ease of doing business will drastically changed with the introduction.
- GDP will improve by 1% to 2%.
- Hope & Pray GST is be introduced after giving sufficient time for preparation to the stakeholders.

