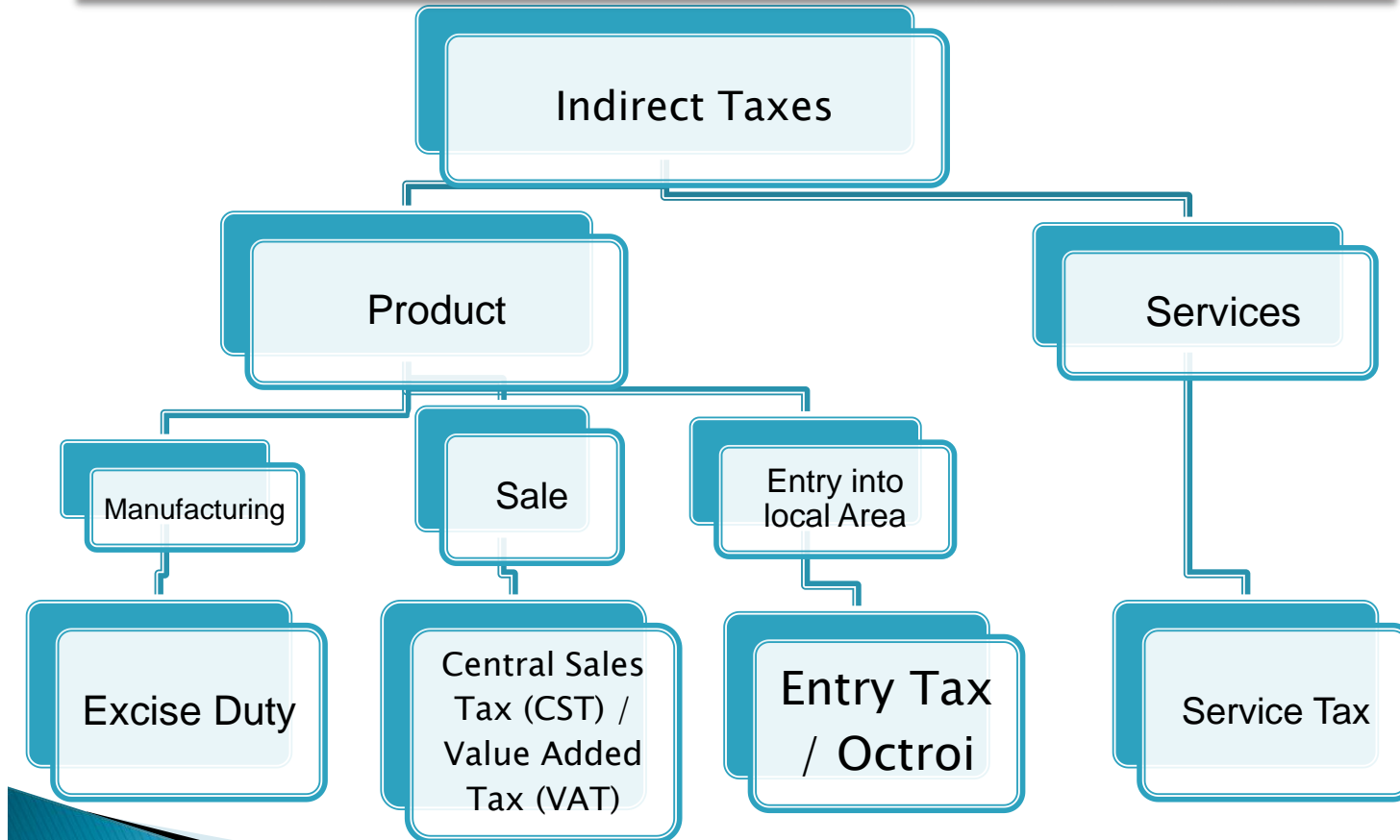


# Presentation on Works Contract Tax

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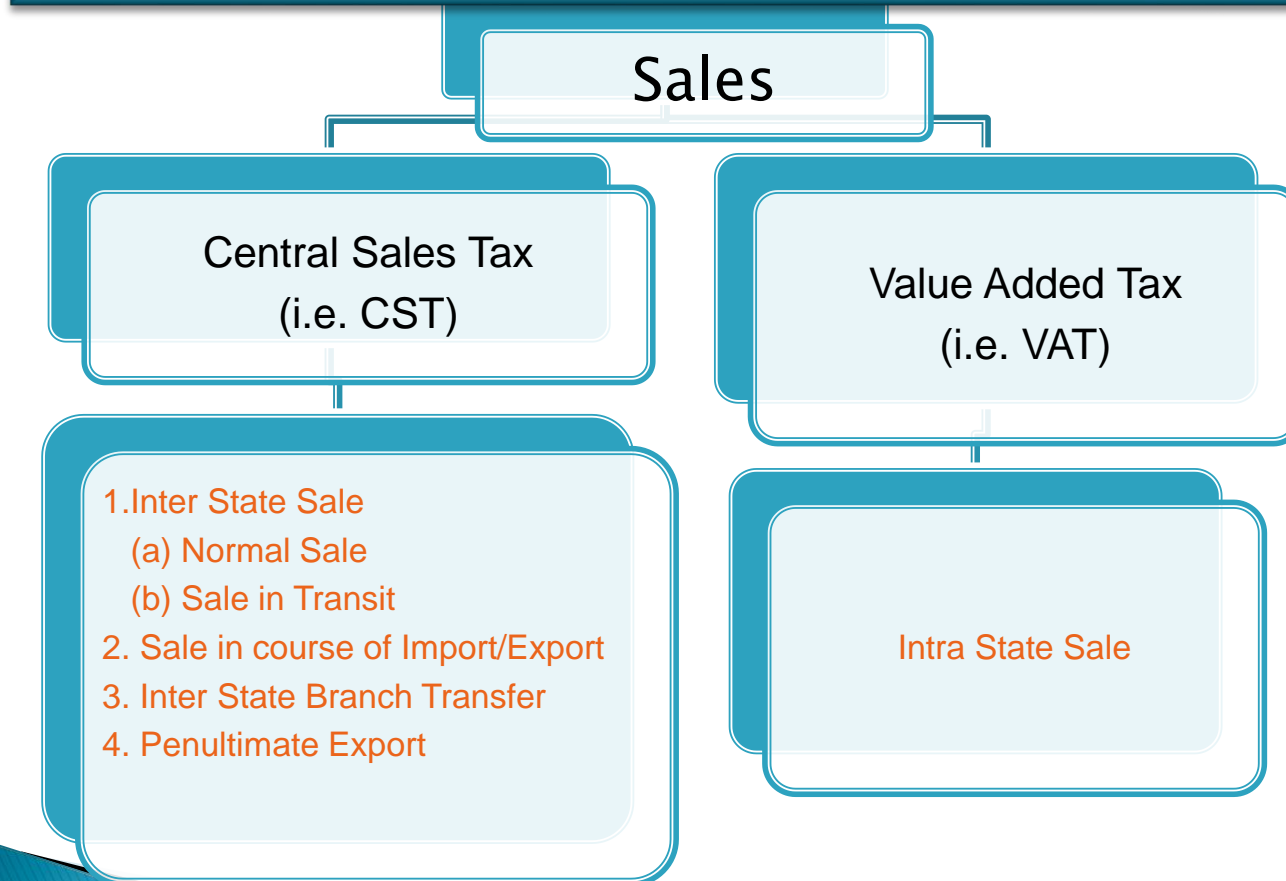
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## Indirect Taxes



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## **Categories of Sales**



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## **SALE - Meaning**

▶ “Sale” means:

- any transfer of property in goods;
- for cash , deferred payment or other valuable consideration;

and includes:

- *Transfer of property in goods involved in Works Contract,*
- Hire purchase transaction;
- Sale to member of unincorporated association/body/person
- Transfer of right to use;
- Transfer of property, otherwise than in pursuance of a contract for a consideration (i.e. Compulsory Sale);
- Sale of food articles as a part of service.

Deemed Sales

## *What is Works Contract*

**Works Contract** means a contract for carrying out any work which includes

assembling,	construction,
building,	altering,
manufacturing,	processing,
erection,	installation,
fitting out,	improvement,
repair or	commissioning

of any **movable or immovable** property.

- **Above definition is as per CST Act and almost similar in various State Acts**

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## Legislative History of Works contract

### State of Madras Vs GDC (1959) 9 STC 353 (SC)

- Sales tax only on sale as per Sale of Goods Act
- All conditions of sale as per Sale of Goods Act to be satisfied
- No tax in case of indivisible works contract – no sale as no agreement to sell materials

### (Dominant Nature Test theory propounded)

- Property does not pass as movable
- Building contract – one, entire and indivisible
- Splitting of contract to isolate value of material not permissible

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## Legislative History of Works contract

- States craved for more revenue
- Constitution amended in 1982
- 46th Constitutional amendment inserted clause 29A to Article 366
- States amended their sales tax legislations to incorporate tax on transfer of property in goods involved in execution of works contracts
- However CST Act was amended in 2002

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## Clause 29A to Article 366

### (29A) "tax on the sale or purchase of goods" includes ;

(a) a tax on the transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration ;

### (b) a tax on the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract ;

(c) a tax on the delivery of goods on hire-purchase or any system of payment by installments ;

(d) a tax on the transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration ;

(e) a tax on the supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration ;

(f) a tax on the supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service is for cash, deferred payment or other valuation consideration,

and such transfer, delivery or supply of any goods shall be deemed to be a sale of those goods by the person making the transfer, delivery or supply and a purchase of those goods by the person to whom such transfer, delivery or supply is made ;

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## Effect of Constitutional Amendment

- ▶ Even indivisible contract now becomes divisible by legal fiction
- ▶ States now empowered to levy tax on deemed sale of materials by splitting by legal fiction
- ▶ However divisible contracts were taxable even earlier
- ▶ BSNL judgement – only transactions covered by 29A (b & f) are permitted to be split
- ▶ Dominant nature test continue to apply to other transactions like Hospital services, lawyers services

## Works contract Vs Sale

- Determination as to whether a contract is works contract or sale is very important
  - For transfer of property and tax jurisdiction
- Works contract transactions involve various special provisions of VAT law like:
  - TDS, TDS No. & TDS Return
  - Composition options
  - Determination of deductions
  - Choice of method of taxation  
(Fixed deduction, composition, actuals)
  - Deductions for subcontracting etc
  - Rates of taxes (some states have flat **12.50% to 14.5% VAT Rate** for works contracts)
  - Different Basic Exemption limits for WCT

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# Sale or works Contract

- Where main object of the work undertaken for a price is not the transfer of chattel qua chattel, the contract is one for work and labour.

## Kone Elevators (SC)

- No straight jacket formula to determine whether a contract is a contract of sale or one for work or labour and service

- Facts of the case, construction of terms and conditions of the contract between the parties, intention of the parties, not mere form but the substance of the contract have to be looked into

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## **Sale vs. Works Contract**

<b>Sales of Goods</b>	<b>Works Contract</b>
It is 'sale simpliciter'	Transfer of property in goods involved in works contract is ' <b>Deemed Sale</b> ', divisible only through fiction of law
Contract is <b>primarily for supply of materials</b> ; work or service is incidental to execution of contract.	Contract is <b>primarily for work and labour</b> , materials are supplied in execution of such contract.
Thing produced/manufactured as a whole is <b>absolute property of the maker when comes into existence, transferred to the buyer later under contract of sale.</b>	Thing produced/manufactured as a whole <b>directly become the property of buyer without becoming property of maker.</b>
Property passes by transfer at the time of delivery of finished article as a chattel	Transfer of property is at the time of procession of work by accession (immovable property) or fusion with movable property of customer

## Transfer of property – **Sale of Goods Act**

**Section 19 – Property to transfer at time when parties to contract intend it to transfer**

- **Section 23 – In case of future/unascertained goods, property passes when goods are unconditionally appropriated to the contract –**

- **goods in deliverable state when delivered to carrier are said to be unconditionally appropriated unless seller reserves the right of disposal.**

- **"Ordinarily unless there is a contract to the contrary in the case of works contract the property in the goods used in the construction of a building passes to the owner of the land on which the building is constructed, when the goods or materials used are incorporated in the building."** {Builders' Association of India and others v. Union of India and others – [(1989) 73 STC 370]}

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## Divisible Contract Vs Indivisible Contract

- No straight jacket formula to distinguish between a divisible and indivisible works contract

Imagic Creative Pvt. Ltd. Versus Commissioner of Commercial Taxes & Ors. (DATE OF JUDGMENT: 09/01/2008)

The Supreme Court observed:

A distinction must be borne in mind between an indivisible contract and a composite contract.

## Divisible Contract Vs Indivisible Contract

• AP High Court – [2003] 132 STC 0272– – Larsen & Toubro Limited Vs. Commissioner of Commercial Taxes (and other cases)

• that the entire project work had to be completed by the appellant which included installation of machinery and supervision up to certain point of time.

• that is to say, the contract was composite in nature.

• By merely supplying material to the contractee, the responsibility arising out of the agreement did not cease

• the appellant had to install the machinery and watch the performance for a period of 15 months.

• Certain goods were manufactured by the appellant on the specification of the contractee at the factory near Bombay and the representatives of the contractee inspected the goods and after being satisfied with the quality of goods clearance was given.

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## Divisible Contract Vs Indivisible Contract

- 90 per cent of the value of goods was already received by the appellant from the contractee.
- The movement of goods was occasioned pursuant to the contract.
- The documents on record would go to show that these goods had reached the destination as per the terms of the contract.
- Central sales tax was paid to the State of Maharashtra under the scheme of the Act.
- Having regard to the fact that there were two facets of the contract, supply of goods and installation of machinery with the labour of the appellant, the contract was a divisible contract.
- The transaction was an inter-State transaction and not an intra-State transaction and the turnover arising on this transaction could not be brought under local sales tax

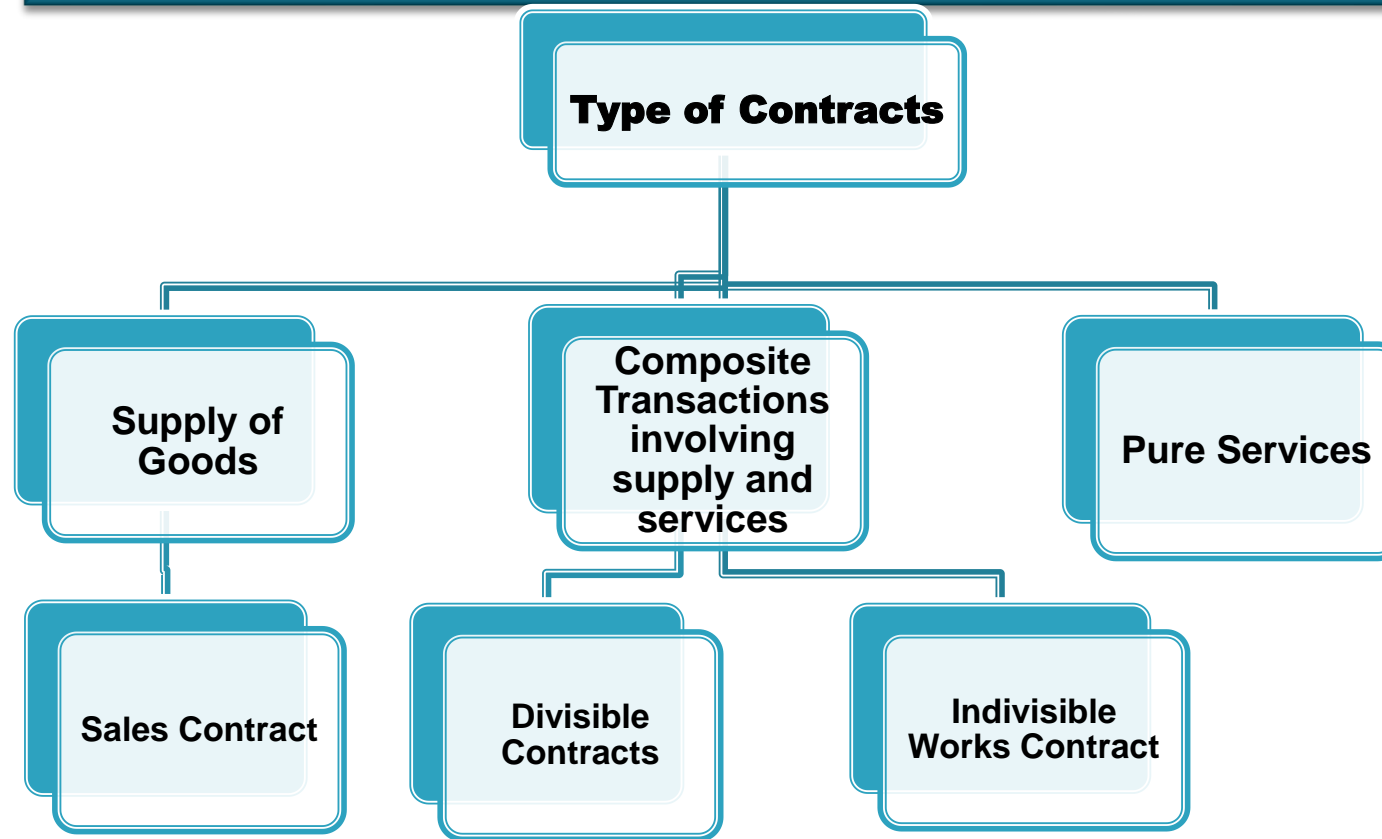
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# Taxability

- Tax on materials involved
- Tax not on works contract
- No tax if no materials involved – pure labour/service contracts

## **Categories of Contracts**



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## **Methods for paying Works Contract- VAT**

<b>Modes</b>	<b>Remarks</b>
<b>1. Composition Scheme</b>	<b>Pay WCT at fixed % of contract price</b>
<b>2. Regular Assessment Mode</b>	<b>Deduct eligible expenses from Contract Value and pay WCT on actual value of materials as per State VAT rate</b> (Charges for labour & Service, cost of establishment, overheads, consumables etc & profit element related thereto)
<b>3. Standard Deduction Mode</b>	<b>Deduct prescribed percentage of CV as per State VAT – pay tax on balance at higher VAT rate</b>

## **Computation of WCT – Actuals /Std Deduction**

### **Computation of VAT**

**Depends upon State Provisions**

#### **1. Calculate Total Turnover**

Aggregate of contract price

#### **2. Less : permissible Deductions**

1. Charges for labour & Service, cost of establishment, overheads, consumables etc & profit element related thereto (**Regular Asstt mode**)
2. Fixed Percentage as per State VAT (**Std ded**)

#### **3. Compute Output Tax**

Declared goods- maximum rate 5%  
Other Goods – as per State VAT Schedule

#### **4. Less: Input Tax Credit**

Tax paid on local eligible purchases of goods

#### **5. Adjustment of WCT TDS**

#### **6. Result - Net Tax Payable**

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## **Other aspects of Works Contract- VAT**

- Tax Deduction at Source
- Obtaining TDS No
- Filing of TDS returns
- Issuing WCT certificates to contractors
- No deduction from CST sales
- No deductions from pure service contracts
- Interest/Penalty liability in case of non deduction or not remitted to Department as per State provision.
- Nil or lower deduction in case contractor submits certificate issued by Commercial Tax Department.

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## **Composition Scheme for Works contract**

- ▶ Tax to be paid at specified % on total value of contract.
- ▶ Dealers opting for Composition scheme generally **not permitted** :
  - To raise Tax invoice.
  - To avail ITC.
- ▶ Effective tax generally higher in Composition Schemes.
- ▶ Many States have year based composition schemes rather than contract based.

# Works Contract Provisions

Bihar



## **Works Contract Provisions as per Bihar VAT ACT, 2005**

**“Works Contract”** means any agreement for carrying out for cash or deferred payment or other valuable consideration the:

construction,        fitting out,  
improvement or,    repair

of any building, road, bridge or other **movable or immovable** property.



## **Methods for paying Works Contract- Bihar VAT**

Modes	Remarks
1. Composition Scheme	(i) Gross Turnover not to exceed <b>Rs. 40 lacs</b> during a F/Y (ii) Import from outside the State of Bihar not permissible (iii) Project-wise option not available (iv) Pay WCT at fixed 4% of contract price (V) No ITC, NO SCT deduction except labour
2. Regular Assessment Mode	Deduct eligible expenses from Contract Value and pay WCT on actual value of materials as per VAT Schedule
3. Standard Deduction Mode	No Specific Provision

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## **Computation of Taxable Turnover in case of Works Contract- Deductions available**

Following deductions for cost incurred for execution of Works Contract:

- (a) **labour charges** ;
- (b) **amount paid to sub-contractor** on account of labour and services;
- (c) charges for **planning, designing and architect's fees**;
- (d) charges for obtaining on **hire machineries and tools**;
- (e) **cost of consumables** such as water, electricity, fuels etc.;
- (f) **cost of establishment** of the contractor; to the extent related to labour & Services
- (g) other similar expenses;
- (h) **profit earned** by the contractor;
- (i) Goods or transactions exempted u/s 6 or Section 7 of the VAT Act.

## **WCT TDS- Bihar VAT**

- ▶ Contractee / principal liable to deduct tax @ 5% from the amount payable in respect of transfer of property in goods (after deductions towards labour & services) during execution of Works Contract.
- ▶ No TDS on advance payment.
- ▶ NO TDS on payment/part payment where no transfer of property (41(2) (a)- second proviso & Rule 29(2)) like labour charges etc
- ▶ NIL deduction certificate can be obtained from Deptt.

# Works Contract Provisions

## Jharkhand



## **Works Contract Provisions as per Jharkhand VAT ACT, 2005**

**“Works Contract”** means and includes any agreement for carrying out for cash or deferred payment or other valuable consideration for:

assembling,	construction,
fabrication,	erection,
installation,	modification,
fitting out,	improvement,
or repair	

of any building, road, bridge or commissioning of any other **immovable or movable** property.

## **Methods for paying VAT on Works Contract- Jharkhand VAT**

Modes	Remarks
1. Composition Scheme	(i) Import from outside the State not permissible (ii) 4% of contract price (iii) No ITC available, Tax invoice cannot be issued (IV) No specific provision for contract based composition (V) Year based scheme and not contract based
2. Regular Assessment Mode	1. Deduct eligible expenses from Contract Value and pay WCT on actual value of materials as per VAT Schedule 2. SCT to issue Tax invoice to Main Contractor
3. Standard Deduction Mode	(i) Deduct prescribed % of CV as per Sec. 22(2)– pay tax @14% on balance (ii) <b>No ITC available, Tax invoice cannot be issued</b>

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## **Computation of Taxable Turnover in case of Works Contract- Deductions available**

Following deductions for cost incurred for execution of Works Contract:

- (a) **labour charges** ;
- (b) charges for **planning, designing and architect's fees**;
- (c) charges for obtaining on **hire machineries and tools**;
- (d) **cost of consumables** such as water, electricity, fuels etc.;
- (e) **cost of establishment** of the contractor; to the extent related to labour & Services
- (f) other similar expenses;
- (g) **profit earned** by the contractor;

**Note:** Value of goods used in execution of works contract shall **not be less than purchase value** and includes, loading and unloading, transportation and distribution charges etc.

## **WCT TDS- Jharkhand VAT**

- ▶ Contractee/ principal liable to deduct tax @ 4% from the amount payable where transfer of property in goods involved.
- ▶ TDS on gross after deductions for labour and like charges
- ▶ No TDS where no transfer of property is involved.
- ▶ No TDS on inter-state/import/export transaction.
- ▶ No TDS on advance payment.
- ▶ No TDS from composition contractors
- ▶ NIL deduction certificate can be obtained from Deptt for each specific work orders.
- ▶ No TDS if payment not likely to exceed Rs one Lakh.

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Description	Vendor 1	Vendor 2
Type	Local	CST
Basic Price	203	207
VAT/CST	10 (VAT)	4 (CST)
Freight	1	2
Price for Evaluation ?	204	213
Price for Evaluation ?	214	213

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Description	Sale Price	Sale Price
	(VAT)	(CST)
	Excluding Tax	
	270	270
VAT/CST	13	0
Total Billing	283	270
Less Input Credit	10	0
Additional Net Tax	3	0
Net Purchase Cost to Buyer including VAT/CST	204	213

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Description	Sale Price	Sale Price
	(VAT)	(CST)
	Including Tax	
	257	270
VAT/CST	13	0
Total Billing	270	270
Less Input Credit	10	0
Additional Net Tax	3	0
Net Purchase Cost to Buyer including VAT/CST	217	213

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# Thank You



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