

SERVICE TAX- IMPORTANT CHANGES PROPOSED IN UNION BUDGET 2016

The Union Budget 2016 has proposed many changes in the area of service tax. Some of the changes are quite extensive (as in the case of Cenvat Credit Rules, 2004).

This note sets out the important changes in the act, rules and regulations relating to service tax. This note is general in nature and more detailed notes will be issued in due course on some of the critical changes (for example, on the levy of Krishi Kalyan Cess).

We believe that this note will be of assistance to Compliance/Finance teams in order to help them understand the changes that have been proposed. This note does not deal with all the proposed changes but only the ones we consider to be of more relevance.

Please consult your Tax advisors/Accountants etc. before taking any decision based on this note.

LEVY OF KRISHI KALYAN CESS

A new cess, called KRISHI KALYAN CESS, is proposed to be levied from 01.06.2016 @ 0.50% on the value of all taxable services. The manner of calculation of this cess shall be the same as in the case of the Swachh Bharat Cess. Although it is expected that this cess shall be available for claiming cenvat credit, the relevant notification is yet to be issued.

APPROVED VOCATIONAL EDUCATION COURSE

“Approved vocational education course” was defined in section 65B(11). These courses were a part of the “Negative List of Services” defined under section 66D. The Budget proposes to delete the definition in section 65B(11). It also proposes to remove the following from the Negative List of Services:

- a. Pre-school education and education up to higher secondary school or equivalent;
- b. Education as a part of the curriculum for obtaining a qualification recognized by any law for the time being in force;
- c. Education as part of an approved vocational education course.

However, it proposes to include/continue with these in the Mega-Exemption Notification 25/2012 that was first issued on 20th June, 2012. The details are set out later in this note.

The above shall take effect from the date of coming into force of the Finance Act, 2016.

DISTRIBUTION OR SELLING OF LOTTERIES

The definition of “Service” in section 65B(44) excludes a transaction in money or actionable claim. The expression “transaction in money or actionable claim” excludes, as per Explanation 2(ii)(a) to section 65B(44), the activity carried out by a lottery distributor or selling agent in relation to promoting, marketing, organizing, selling of lottery or facilitating in organizing lottery of any kind in any manner.

The Budget proposes to insert the words “on behalf of the State Government” between the words “agent” and “in”.

As per the Lotteries (Regulation) Act, 1988, State Governments shall sell tickets either itself or through distributors and/or agents. Any contract that does not comply with this will be *ultra vires* the Indian Contract Act, 1872.

The Budget proposes to clarify that the activity carried out by the distributors or agents of the State Government shall be liable to service tax.

The above shall take effect from the date of coming into force of the Finance Act, 2016.

SERVICES USING STAGE CARRIER

The service of transportation of passengers, with or without accompanied belongings, by a stage carrier was listed under the Negative List of Services in section 66D. This is now being omitted w.e.f. 01st June, 2016. Therefore, w.e.f. 01st June, 2016, the service of transportation of passengers as aforesaid shall be liable to service tax. However, the services by a stage carrier that is not air-conditioned is being included in the Mega Exemption Notification. See later in this note for details.

TRANSPORTATION OF GOODS FROM OUTSIDE INDIA TO CUSTOMS STATION OF CLEARANCE IN INDIA

The service of transportation of goods by an aircraft or a vessel from outside India up to the customs station of clearance in India features in the negative list. It is proposed to delete this from the Negative List of Services in section 66D w.e.f. 01st June, 2016. However, for the aforesaid service by way of aircraft, it is being introduced in the Mega-Exemption List and shall, therefore, continue to be exempt from service tax for the time being. See later in this note for details. The services of transportation of goods by vessel shall, therefore, become taxable w.e.f. 01st June, 2016.

ASSIGNMENT OF RIGHT TO USE RADIO-FREQUENCY SPECTRUM AND SUBSEQUENT TRANSFERS TO BE A “DECLARED SERVICE”

It is proposed to declare the assignment by the Government of the right to use radio-frequency and subsequent transfers thereof as a “Declared Service” and these shall not, therefore, be treated as a sale of goods. Section 66E is, therefore, proposed to be amended. The tax payable would be payable on reverse charge (being taxes in respect of services provided by the government) and the manner of treatment of the cenvat credit in such cases is dealt with later in this note.

CHANGES IN ABATEMENT RATES AND CONDITIONS

The abatement represents the reduction of the value of services for the purpose of computing the taxable value of services. The abatement notification was first issued vide Notification No. 26/2012-ST dt. 20th June, 2012 and has since undergone changes. The following changes have now been notified vide **Notification No. 8/2016-Service Tax dt. 01st March, 2016**:

Description of taxable services	Abated value (%)	Conditions
Transport of goods by rail by Indian Railways.	30%	Cenvat Credit on inputs and capital goods, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004. Note: Cenvat Credit on input services can be availed.
Transport of goods by rail by any person other than Indian Railways but not in containers,	30%	Same as above
Transport of goods by rail in containers by any person other than Indian Railways.	40%	Same as above
Transport of passengers with or without accompanies belongings by rail	30%	Cenvat Credit on inputs and capital goods, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004. Note: Cenvat Credit on input services can

Description of taxable services	Abated value (%)	Conditions
		now be availed.
Service of goods transport agency in relation to transportation of goods other than used household goods.	30%	Cenvat Credit on inputs, capital goods and input services, used for providing the taxable service, has not been taken by the service provider under the provisions of the Cenvat Credit Rules, 2004. Note that cenvat credit on input services is not available in this case. Note further that this abatement does not apply for household goods that are used. However, it applies for household goods that are new (for example, where new household goods are purchased directly from a dealer/distributor/shop and transported by a Goods Transport Agent).
Services of goods transport agency in relation to transportation of used household goods.	40%	Same as above (except the notes).
Services provided by a foreman of a chit fund in relation to chit.	70%	Same as above (except the notes)
Transport of passengers with or without accompanied belongings by a stage carrier. (with effect from 01st June, 2016).	40%	Same as above (except the notes)
Transport of goods in a vessel.	30%	Cenvat Credit on inputs and capital goods, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules,

Description of taxable services	Abated value (%)	Conditions
		2004. Note: Cenvat Credit on input services can now be availed.
Services of a tour operator in relation only to arranging or booking of accommodation for any person.	10%	<p>Cenvat Credit on inputs, capital goods and input services, used for providing the taxable service, has not been taken by the service provider under the provisions of the Cenvat Credit Rules, 2004. However, Cenvat Credit of input services of a tour operator may be availed.</p> <p>The invoice, bill or challan that is issued indicates that it is towards the charges for the accommodation,</p> <p>The abatement shall not apply where the invoice, bill or challan issued by the tour operator includes only the service charges for booking but does not include the charges for the accommodation.</p>
Services of tour operator other than for booking accommodation.	30%	Cenvat Credit on inputs, capital goods and input services, used for providing the taxable service, has not been taken by the service provider under the provisions of the Cenvat Credit Rules, 2004. However, Cenvat Credit of input services of a tour

Description of taxable services	Abated value (%)	Conditions
		<p>operator may be availed.</p> <p>The bill issued for this purpose indicates that it is inclusive of charges for such a tour and the amount charged in the bill is the gross amount charged for such a tour.</p>
<p>Construction of a complex, building, civil structure or a part thereof, intended for sale to a buyer, where entire consideration is received on or before the issuance of completion certificate by the competent authority.</p>	<p>30%</p>	<p>Cenvat credit on inputs used for providing the taxable service has not been taken under the provisions of the Cenvat Credit Rules, 2004. Note that Cenvat Credit on capital goods and input services may be taken.</p> <p>The value of the land is included in the amount charged from the service receiver.</p>

In the case of abated value for renting of motorcab, the abated value continues to be 40%. However, the value of services shall now include the fair market value of goods (including fuel) and services supplied by the recipient of services in or in relation to the service, whether supplied under the same contract or any other contract. In other words, where the service provider has executed a separate contract for the provision of driver, fuel etc., then the value of these, in relation to the relevant motorcab, shall also be included in the value of services on which abatement is to be computed.

The services of tour operator having now been split into two- that is, services for accommodation and others, the definition of “package tour operator” in paragraph 2(b) of the Notification No. 26/2012 has been deleted.

Except in the case of abatement on stage carrier, all other changes mentioned in the above table and notes below the table take effect from 01st April, 2016.

CHANGES IN MEGA-EXEMPTIONS AND CONDITIONS

Vide Notification Number 25/2012-Service Tax, Mega Exemptions were notified. The notification has undergone several changes (by way of additions, deletions and clarifications) since then and, at present, is made up of 47 exemptions.

The Budget 2016 has now amended the Mega Exemptions (Notification Number 9/2016-Service Tax dt. 01st March, 2016 refers) once again and the **changes take effect from 01st April, 2016 unless specified otherwise**. The changes are summarized below:

- a. Services provided by a Senior Advocate by way of legal services to any a person (other than a person ordinarily carrying out any activity relating to industry, commerce or any other business or profession), shall be exempted. This means that the legal services provided by a senior advocate to any other advocate, firm of advocates, firm of chartered accountants, cost accountants, business entities etc shall be taxable.
- b. Services provided by the IIM's, as per the guidelines of the Central Government, to their students, towards the following educational programmes (except the Executive Development Programme) shall be exempt from service tax:
 1. Two year full time PG Diploma in Management (commonly referred to as MBA), admissions to which are on the basis of CAT;
 2. Fellowship programme in Management;
 3. Five year integrated programme in Management.

This shall be applicable from 01st March, 2016.

- c. Services of assessing bodies empanelled centrally by the Directorate General of Training, Ministry of Skill Development and Entrepreneurship, by way of assessments under the Skill Development Initiative (SDI) Scheme shall be exempt from service tax.
- d. Services provided by training providers (Project Implementation Agencies) under the Deen Dayal Upadhyaya Grameen Kaushalya Yojana under the Ministry of Rural Development by way of offering skill or vocational training courses certified by the National Council for Vocational Training shall be exempt from service tax,

- e. Services provided by an artist by way of a performance in folk or classical art forms of music or dance or theatre, if the consideration charged for the performance is not more than INR 150,000 shall be exempt from service tax. At present, the limit is INR 100,000 and the Budget seeks to merely increase this limit. **However, this exemption shall not apply where the artist is a brand ambassador.**
- f. Transport of passengers with or without accompanied belongings by a non-air conditioned stage carrier shall be exempt from service tax. **However, this exemption shall take effect from 01st June, 2016.**
- g. Transport of passengers with or without accompanied belongings by ropeway, cable car or aerial tramway shall no more be exempt from service tax.
- h. Services of general insurance business provided under the “Niramaya Health Insurance Scheme implemented by the Trust constituted under the National Trust for the Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities Act, 1999 shall be exempt from service tax.
- i. Life insurance services provided by way of annuity under the National Pension System regulated by the PFRDA shall be exempt from service tax.
- j. Services provided by the EPFO, IRDA (to insurers), SEBI, and the National Centre for Cold Chain Development (by way of knowledge dissemination on cold chain) shall be exempt from service tax.
- k. Services by way of transportation of goods by an aircraft from a place outside India up to the customs station of clearance in India shall be **exempt from service tax w.e.f. 01st June, 2016.**

CHANGES IN POINT OF TAXATION

The Point of Taxation Rules, 2011 were notified on 01st March, 2011. The power to define the point of taxation is obtained from section 94(2)(a) and (hhh).

Section 67A of the Finance Act, 1994 deals with the date of determination of rate of tax, value of taxable service and rate of exchange. In order to obtain specific rule making power in relation to point of taxation, section 67A is proposed to be amended from the date of coming into force of the Finance Act, 2016 to give power to prescribe the point in time with respect to the rate of service tax.

The Point of Taxation Rules, 2011 shall be amended as follows:

- a. From the date of coming into force of the Finance Act, 2016, the Central Government shall have power under section 67A(2) and section 94(2)(a) and 94(2)(hhh) to make rules for the purpose of collection of and determination of rate of service tax.
- b. Explanation 1 is being inserted below Rule 5 to provide that Rule 5 shall apply in case of new levy on services. In other words, Rule 5 will govern the charge of Krishi Kalyan Cess w.e.f. 01st June, 2016, for example. **The insertion of Explanation 1 will take effect from 01st March, 2016.**
- c. Explanation 2 is being inserted below Rule 5 to provide new levy or tax shall be payable in all cases other than the ones on which it is not payable as per Rule 5. **The insertion of Explanation 2 will take effect from 01st March, 2016.**

In this connection, it may be noted that the proposed Explanation 1 refers only to new levy whereas the proposed Explanation 2 refers both to new levy or tax. The reason for this is simply explained: Rule 5 deals with payment of tax in case of services taxed for the first time. The Explanation 1, therefore, proposes to treat a new levy on the same footing as a service that is proposed to be taxed for the first time. The Explanation 2, however, deals with situations in which the new levy, or the tax (on services that are to be taxed for the first time) will apply. It clarifies that except for cases where: (a) invoice has been issued and payment received against the invoice before the service becomes taxable; and (b) payment has been received before services becomes taxable and invoice is issued within 14 days of the date on which the service became taxable, in all other cases, tax shall be payable.

It may further be noted that for services that were already taxable (that is, services that are not being taxed for the first time), the levy of Krishi Kalyan Cess shall be governed by Rule 5 whereas for the same services, where the effective rate of taxation is being changed due to changes in abatement notification, the new effective rate of tax shall be governed by Rule 4. This distinction is very important to understand.

Notification No. 10/2016-Service Tax dt. 01st March, 2016 refers.

CONDITIONAL EXEMPTION TO CERTAIN INFORMATION TECHNOLOGY SOFTWARE SERVICES

Services in relation to Information Technology Software constitute a Declared Service under section 66E. Where the Information Technology Software is recorded on a media under Chapter 85 of the Central Excise Tariff Act, 1985, on which the Retail Sales Price is required to be declared, then central excise duty / appropriate customs duty is required to be paid. Therefore, in such cases, both service tax and central excise duty/customs duty becomes leviable.

To remove this anomaly, a conditional exemption from service tax has been notified for Information Technology Software recorded on a media under Chapter 85 aforesaid. The applicable conditions are:

- a. The software recorded on the media is covered by the Legal Metrology Act, 2009, requiring disclosure of Retail Sales Price;
- b. The value of the package of such media has been determined; and
- c. The appropriate excise duty or customs duty has been paid;
- d. A declaration is made by the service provider on the invoice that no amount in excess of the retail sale price declared on such media has been recovered from the customer.

The exemption is valid from 01st March, 2016 and Notification No. 11/2016-Service Tax dt. 01st March, 2016 refers.

CHANGES IN INTEREST RATES U/S 75

Section 75 deals with interest on delayed payment of service tax. As it presently stands, delay in payment of service tax attracts interest varying between 18% p.a. to 30% p.a. depending upon the period of delay. By virtue of proviso to section 75, a service provider whose value of taxable services does not exceed INR 60 Lakhs shall be entitled to an abatement of 3%- in other words, the interest shall be varying between 15% p.a. and 27% p.a.

The Budget proposes the following **changes w.e.f. the date of coming into force of the Finance Act, 2016:**

- a. Where any amount has been collected as service tax but not paid on or before the due date on which the payment becomes due: 24% p.a.;
- b. In other cases of delay: 15% p.a.

For a service provider whose value of taxable services does not exceed INR 60 Lakhs, the corresponding rates shall be 21% p.a. and 12% p.a. respectively.

Notification Number 13/2016-Service Tax dt. 01st March, 2016 refers.

CHANGES IN INTEREST RATES U/S 73B

Section 73B deals with interest payable where service tax has been collected in excess but the excess collected is not paid to the Central Government- that is, interest in cases of unjust enrichment. As it presently stands (vide Notification No. 15/2011-Service Tax dt. 01st March, 2011), the rate of interest payable is 18% p.a. Under certain conditions, for a service provider whose value of taxable services does not exceed INR 60 Lakhs, the interest shall be 15% p.a.

The Budget proposes to reduce the interest rate from 18% p.a. to 15% p.a. For a service provider whose value of taxable services does not exceed INR 60 Lakhs, the corresponding rate shall be 12% p.a. The change shall be **w.e.f. the date of coming into force of the Finance Act, 2016.**

Notification No. 14/2016-Service Tax dt. 01st March, 2016 refers.

SUPPORT SERVICES PROVIDED BY GOVERNMENT OR LOCAL AUTHORITY

Under section 66D(a), services provided by Government or local authority were in the negative list of services. However, it excluded “support services” provided to business entities. In other words, “support services” provided by Government or local authority were not in the negative list of services.

The **Finance Act, 2015** had omitted the definition of “support services” in section 65B(49). Consequentially, the expression “support services” in section 66D(a) was replaced by the expression “any service”. The date from which the changes were to take effect were to be notified.

The aforesaid changes come into effect from 01st April, 2016. Notifications No. 15/2016-Service Tax and 16/2016-Service Tax, both dated 01st March, 2016 refer.

CHANGES IN REVERSE CHARGE MECHANISM

Notification No. 30/2012-Service Tax dt. 20th June, 2012 specifies the services on which tax is payable on reverse charge basis by the person (other than the service provider) who is liable to pay the service tax. This notification was last amended by Notification No. 7/2015-Service Tax dt. 01st March, 2015.

The changes proposed in the Budget 2016 are mainly consequential upon changes proposed in other sections/rules. **They come into force on 01st April, 2016** and are summarized below:

- a. Taxable services provided or agreed to be provided by a mutual fund agent or distributor, to a mutual fund or asset management company shall no more be under reverse charge mechanism.
- b. Consequential changes have been made due to changes in the case of selling or marketing agents of lottery tickets (refer page 1 “Distribution or selling of lotteries”) and services of senior advocates (refer page 7 under “Changes in Mega-Exemptions and conditions”).
- c. Services provided by Government or local authority other than those in Negative list and (i) renting of immovable property; (ii) services of department of Posts specified in section 66D(a)(i); (ii) services in relation to an aircraft or a vessel, inside or outside the precincts of a port or an airport specified in section 66D(a)(ii); and (iii) transport of goods or passengers, shall be taxable under Reverse Charge Mechanism.

Notification No. 18/2016-Service Tax refers.

CHANGES IN SERVICE TAX RULES

The following are the important changes in the Service Tax Rules, 1994 and **shall come into force w.e.f. 01st April, 2016 unless otherwise specified:**

- a. For an individual or proprietary firm or partnership, service tax is payable quarterly by the 6th of the immediately following month. This benefit is now being extended to
 1. One Person Company whose aggregate value of taxable services provided in the previous financial year does not exceed INR 50 Lakhs; and
 2. Hindu Undivided Family (HUF).
- b. For individuals and partnership firms whose aggregate value of taxable services provided does not exceed INR 50 Lakhs in the previous financial year, the tax on services provided or agreed to be provided may be paid after collection of payment. This benefit is being extended to One Person Company, too.
- c. In the case of single premium annuity policies, the insurer carrying on life insurance business shall have the option to pay tax of 1.40% of the single premium charged from the policy holder.

- d. In addition to half-yearly returns, an annual return will have to be filed by the 30th November every year. The form and manner of filing shall be notified. However, the Central Government may exempt certain assesseees or class of assesseees from filing this. A revised return of such annual return may also be submitted within a period of one month from the date of filing of the original annual return. Delay in filing of annual return shall attract payment of INR 100 per day of delay subject to a cap of INR 20,000.

Other changes are consequential upon the changes referred to in earlier sections of this note.

Notifications Number 17/2016-Service Tax and 19/2016-Service Tax, both dt. 01st March, 2016 refer.

CHANGES IN CENVAT CREDIT RULES, 2004 (to the extent applicable to service tax assesseees)

Changes proposed in Cenvat Credit Rules, 2004 shall **take effect from 01st April, 2016 unless otherwise specified**. Notification No. 13/2016-Central Excise (N.T.) dt. 01st March, 2016 refers.

The following are the important changes that affect service tax assesseees:

- a. "Exempted services" are defined in Rule 2(3). A service which is exported in terms of Rule 6A shall not be treated as an "exempted service". It is proposed that services by way of transportation of goods by a vessel from customs land station of clearance in India to a place outside India shall also not be considered "exempted service". As a result, reversal of cenvat credit arising from such services need not be made.
- b. All capital goods which have a value up to INR 10,000 per piece shall be treated as "input".
- c. Cenvat credit of service tax paid on the assignment of the right to use radio-frequency spectrum (in fact, any natural resources) can be availed over the period of time for which the right to use has been assigned. The credit in the financial year in which the right to use is assigned, and in subsequent financial years during which the right to use is retained, shall be calculated using the formula "Credit = Service Tax paid /Number of years for which the rights have been assigned. **It may be noted that it is only where the Government is the assignor that reverse charge mechanism applies. If the assignor, however,**

is not the Government, then service tax shall be paid on forward charge basis. Where the assignee (say, Assignee 1) in turn assigns such right to use to another person (say, Assignee 2), then the unutilized portion of cenvat credit available with Assignee 1 may be set off against the service tax payable by Assignee 1 on the consideration charged from Assignee 2, but may not exceed the tax so charged. An example will clarify:

Say Assignee 1 is assigned the right to use by the Government from 01st April 2016 to 31st March, 2021- that is, 5 years. The tax payable on reverse charge basis is 1 crore. Then, as per formula, the cenvat credit that may be claimed each year is INR 1 crore divided by 5 = INR 20 Lakhs each year. Suppose, w.e.f. 01st April 2017, the right to use is assigned by Assignee 1 to Assignee 2 and the service tax on the consideration charged is INR 50 Lakhs. Then, in fiscal 2017-18, Assignee 1 can set off only INR 50 Lakhs (out of balance available of INR 80 Lakhs) as cenvat credit. *Prima facie*, it appears that after such set-off, the balance amount of INR 30 Lakhs will be lost. In the case of annual or monthly user charges payable in respect of any service by way of such assignment, the cenvat credit shall be allowed in the same financial year in which they are paid.

- d. Rule 6, that deals with the obligations of a service provider who provides both taxable and exempted services, is being amended. The amendments are extensive and shall be covered by way of a separate note.
- e. An annual return shall henceforth be filed by the 30th November of the succeeding financial year. The form for the same shall be notified.
- f. The Finance Act, 2015 had introduced FIFO basis for ascertaining which cenvat credit had been availed. This was prescribed in Rule 14(2) for ascertaining cenvat credit wrongly taken (or erroneously refunded) and for recovery thereof. Rule 14(2) is being omitted and the determination of whether a particular credit has been availed or not shall be based on whether the minimum balance of credit available to the assessee during a period is lesser than the disputed amount of credit.

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