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A Brief Note on Reverse Charge Mechanism

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The general principle in service tax is that the service provider is liable for payment of service tax. But, in certain cases, the liability is shifted from the service provider to the service receiver and the same is referred to as reverse charge. As per Notification 30/2012 dated 20.06.2012, the following cases will attract service tax in the hands of service recipients, with effect from 01.07.2012.

Sl. No.	Provider of Service	Recipient of Service	Service provider's liability	Service recipient's liability
1.	Services provided by insurance agents to persons carrying on insurance business	Persons carrying on insurance business (Insurance Companies)	Nil	The entire service tax liability shall be discharged by the service recipient, i.e. the Insurance company
2.	Services provided by Goods Transport Agency	If the person paying freight is:- a) Factory; b) Any registered society; c) Any co-operative society; d) Any dealer registered under CE; e) Any body corporate; f) Any partnership firm, whether registered or not including association of persons.	Nil	The entire service tax liability shall be discharged by the person paying the freight. It is clarified that as per Notification 26/2012, ST is payable only on 25 % of freight. Such liability on 25 % of freight amount shall be discharged in full by the service recipient.
3.	Services provided by Sponsors of events etc. to those sponsoring.	1. Body Corporate; 2. Partnership firm	Nil	The entire service tax liability shall be paid by the service recipient.
4.	Services provided by Arbitral Tribunal	Business entity	Nil	The entire service tax liability shall be

				discharged by the service recipient
5.	Legal Services provided by Individual Advocate or firm of advocates.	Business entity	Nil	The entire service tax liability shall be discharged by the service recipient
6.	Support services provided by Government or Local Authority excluding: 1. Renting of Immovable Property; and 2. Services specified in sub clauses (i), (ii) & (iii) of Clause (a) of Section 66D of the Finance Act: (i) services by the Department of Posts by way of speed post, express parcel post, life insurance and agency services provided to a person other than Government; (ii) services in relation to an aircraft or a vessel, inside or outside the precincts of a port or an airport; (iii) transport of goods or passengers;	Business entity	Nil	The entire service tax liability shall be discharged by the service recipient.
7.	Services by way of renting or hiring of passenger vehicles, provided by 1. Individual; or 2. HUF; or 3. Partnership Firm (whether registered or not including the association of persons);	Business entity registered as a body corporate. (Who are not engaged in the similar line of business)	Nil	As per Notification 26/2012, ST is payable on 40 % of value. Hence, the entire service tax on 40 % of the value shall be discharged by the service recipient.
Suppose if the bill value is Rs.10,000, the service recipient will pay the entire service tax liability on abated value. i.e. on Rs.4,000 (40 % of Rs.10,000), the ST liability of 12 %, i.e. Rs.480 shall be paid by the service recipient. The service provider is not liable to pay any				

service tax.				
8.	<p>Services by way of renting or hiring of passenger vehicles, provided by</p> <ol style="list-style-type: none"> 1. Individual; or 2. HUF; or 3. Partnership Firm (whether registered or not including the association of persons); 	<p>Business entity registered as a body corporate. (Who are not engaged in the similar line of business)</p>	<p>If the service provider does not intend to claim abatement, he has to pay 60% of the total service tax liability. In the above given example, the ST liability on Rs.10,000 @ 12 % is Rs.1,200, out of which the service provider has to pay 60 % of Rs.1,200, i.e. Rs.720</p>	<p>The service recipient shall pay 40 % of the total liability, i.e. Rs.480. It may be noted that in both the cases, the service recipient's liability is same.</p>
9.	<p>Manpower supply services or [security services]* provided by</p> <ol style="list-style-type: none"> 1. Individual; or 2. HUF; or 3. Partnership Firm (whether registered or not including the association of persons); 	<p>Business entity registered as a body corporate.</p>	<p>25% of the Service tax liability shall be paid by the service provider.</p>	<p>75 % of the ST liability shall be paid by the service recipient.</p>
10.	<p>Works Contract services provided by</p> <ol style="list-style-type: none"> 1. Individual; or 2. HUF; or 3. Partnership Firm (whether registered or not including the association of persons); 	<p>Business entity registered as a body corporate.</p>	<p>50 % of the service tax liability shall be paid by the service provider.</p>	<p>50 % of the Service tax liability shall be paid by the service recipient.</p>
<p>Both service provider and service recipient can independently opt for any method, viz., Composition scheme or Rule 2 A of ST Valuation Rules.</p>				
11.	<p>Any service provided by a person located outside the taxable territory (non taxable territory).</p>	<p>Any person located in the taxable territory</p>	<p>Nil</p>	<p>The entire service tax liability shall be paid by the service</p>

				recipient.
12.	Services provided by non employee directors to the company**	Company	NIL	100 %

*security services – reverse charge introduced vide Notifications 45 & 46/2012 ST Dated 07.08.2012.

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The following definitions are relevant to apply the above provisions.

Section 65 B (17) : "**business entity**" means any person ordinarily carrying out any activity relating to industry, commerce or any other business or profession.

Section 65 B (31) "**local authority**" means-

- (a) a Panchayat as referred to in clause (d) of article 243 of the Constitution;
- (b) a Municipality as referred to in clause (e) of article 243P of the Constitution;
- (c) a Municipal Committee and a District Board, legally entitled to, or entrusted by the Government with, the control or management of a municipal or local fund;
- (d) a Cantonment Board as defined in section 3 of the Cantonments Act, 2006;
- (e) a regional council or a district council constituted under the Sixth Schedule to the Constitution;
- (f) a development board constituted under article 371 of the Constitution; or (g) a regional council constituted under article 371A of the Constitution.

Section 65 B (49) : "**support services**" means infrastructural, operational, administrative, logistic, marketing or any other support of any kind comprising functions that entities carry out in ordinary course of operations themselves but may obtain as services by outsourcing from others for any reason whatsoever and shall include advertisement and promotion, construction or works contract, renting of immovable property, security, testing and analysis.

Section 65 B (54) : "**works contract**" means a contract wherein transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods and such contract is for the purpose of carrying out construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, alteration of any movable or immovable property or for carrying out any other similar activity or a part thereof in relation to such property.

Before parting...

It may be noted that in certain cases (receiving services of individual advocates, support services provided by Government, etc), the service recipient's category is mentioned as "business entity" which has to be understood as defined above. This definition may also include an individual or partnership firm, who are engaged in industry, or commerce or business or profession. But in certain other cases (receiving services of manpower supply, rent a cab and works contract), the service recipient's category is mentioned as "business entity registered as body corporate" which would not include individual businessmen and partnership firms.

Reverse Charge on rent a cab – further explained.

The issue of payment of service tax on reverse charge basis in respect of renting of cab services is creating lot of confusion in the field. Let us see an example.

At the outset, the reverse charge will apply, only when the service provider is an individual, HUF, partnership firm or association of persons and the service recipient is a business entity and body corporate.

Let the bill value of the rent a cab operator is Rs.10,000

As per S.No. 9 of Notification service tax is payable on 40 % of the Value. This is subject to non availment of cenvat credit by the service provider.

S.No.	Options	Service providers' liability	Service recipients' liability	Remarks
1	Service provider need not pay any service tax. It will be presumed that he has opted for abatement. The bill issued by the rent a cab operator would not contain any Service tax. He would not have taken any cenvat credit also.	NIL	Rs.480	100 % of the ST liability on 40 % of the total value, i.e. 12 % on Rs.4,000
2	If the service provider has paid service tax without claiming abatement	60 % of the ST liability @ 12 % on Rs.10,000, i.e. Rs.720	Rs.480.	40 % of the total ST liability of Rs.1200.

- It may be noted that if the service provider has opted to avail cenvat credit, he would not be eligible for abatement and hence the total ST liability in this case would be Rs.1,200, out of which Rs.720 will be paid by the service provider and Rs.480 by the service recipient. But, if the service provider has not availed any cenvat credit, he need not pay any service tax at all. The service recipient would pay Rs.480.
- It may also be noted that in both the cases, the service recipients' liability is the same.
- The service providers invoice would not at all contain any service tax if he has not availed any cenvat credit. If he has availed cenvat credit his invoice would show service tax of Rs.720 for a value of Rs.10000 (i.e. 7.2 %).
- In any case, the service recipient can calculate his liability at 4.8 % of the bill value.
- Education CESS and Secondary and Higher Education CESS, etc.
- By mistake, if the service provider continue to show the entire service tax on abated value, i.e. Rs.480 in the above example, he has to be educated that he need not charge any service tax.

