Rule 2A has not considered the expanded definition of works contracts – June 20, 2012

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By S Sivakumar, CA

AS we know, the definition of works contract, in terms of Section 65B(54) of the Finance Act, 1994, in its expanded avatar, includes, works done in respect of movable goods. The expanded definition reads as under:

(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;

Now, let's take a look at the regular definition of works contract, under the VAT Law… I've re-produced below, the definition contained in Section 2(37) of the Karnataka Value Added Tax Act, 2003:

"Works contract" includes any agreement for carrying out for cash, deferred payment or other valuable consideration, the building, construction, manufacture, processing, fabrication, erection, installation, fitting out, improvement, modification, repair or commission of any movable or immovable property ".

It would seem, per se, that the definition of works contract under the service tax law is wider in scope, as compared to that, under the VAT law. So far so good..

In terms of the definition contained in the VAT law, many transactions are considered as works contracts. The Sixth Schedule to the KVAT Act, 2003 lists down some 22 specific entries and also has a residuary item, which talks of transactions notspecifically listed in the Schedule.

Some of the transactions specifically treated as 'works contracts' under the KVAT Act, 2003 are: Programming and providing of computer software, Tyre Re-treading, Service and Maintenance of IT products, Printing, Block making, etc. These transactions should also get included under the expanded definition of works contracts, under the service tax law… Fine.

But, how does the abatement scheme provided in Rule 2A of the Service Tax (Determination of Value) Rules, 2006, in terms of Notification No. 24/2012-ST dated June 6, 2012 work *vis-à-vis* the expanded definition?

As we know, in terms of Rule 2A, works contracts pertaining to 'original works' are treated on a better footing as compared to other works contracts, in terms of the higher abatement percentage of 60% (with service tax being required to be discharged on 40% of the gross amount received), when separate books of accounts are not maintained. The relevant portion of Rule 2A, defining 'original works' is reproduced below:

Explanation 1.- For the purposes of this rule,-
(a) "original works" means-
(i) all new constructions;
(ii) all types of additions and alterations to abandoned or damaged structures on land that are required to make them workable;
(iii) erection, commissioning or installation of plant, machinery or equipment or structures, whether pre-fabricated or otherwise;

One can see that, there is no reference to works contracts related to movable property, as the concept of 'original works' is restricted to immovable property, under the definition of 'original works'.

This seems to be a serious drafting error, which needs to be corrected immediately… as otherwise, the benefit of the higher abatement would be disallowed for a large number of 'original transactions' in the nature of works contracts related to movable property, including software development, fitting out of movable assets, etc. Conceptually… higher abatement is to be given to works contracts related to movable property also, as much as, to immovable property, in so far as 'original works' are concerned…

Will the Board kindly intervene and suitably amend Rule 2A?

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