

PROPOSED HEALTH SERVICES- Impact of Service Tax

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Service tax was brought in to existence in 1994 when 3 services were brought into the net. Today, there are more than 100 categories of service that are covered. If we look at the pattern in which the various services were brought into the tax net we would notice that a particular sector is identified and then one by one all kinds of services that can be taxed are made into taxable services. One example would be the construction industry wherein the following are the services taxed with the respective date of introduction of levy:

S No	Service	Date of introduction levy
1	Erection, Installation and Commissioning service	01.07.2003
2	Commercial or Industrial construction	10.09.2004
3	Construction of complex service	16.06.2005
4	Site formation and clearance, excavation and earthmoving and demolition services	16.06.2005
5	Works contract service	01.06.2007
6	Builders Special Service	Proposed in Finance Bill, 2010

The new industry that is targeted is the Health Industry. In the year 2009 Cosmetic and Plastic Surgery service was introduced to the levy. This covered a very small fraction of, the host of health services provided in India. Vide the Finance Bill, 2010 it is proposed to tax health check-up, preventive care and treatment services provided by the hospitals, nursing homes and multi-specialty clinics if payment is made directly by a business entity or Insurance company. This is the first step to tax this service fully in time to come.

GST is round the corner where it is expected that most of the services would be taxed and only a negative list of services, which would not be taxed, would be available.

Thus it is the right time for this industry to start looking at planning its indirect taxes. This is all the more important due to the magnitude of the tax, which would be required to be paid on the revenue as against on profits for the direct taxes and further the strict penalty provisions available thereunder wherein it would be advisable to follow the law rather than pay penalties equivalent to the tax liability.

TAXABLE SERVICE

Let us now discuss a few of the important aspects of service tax which would be handy in tax planning. First of all the definition of taxable service is of utmost importance to identify whether the service provided is a taxable service or not. Taxable services are defined in section 65(105) of the Finance Act, 1994. The definition consists of the following parts:

- a. Service provider
- b. Service receiver
- c. Service sought to be taxed
- d. Exclusion or conditions, if any

For a service to be taxable all the above four criteria should be satisfied. There could be instances where the service receiver and the activity are as defined in the taxable service definition but the service receiver is not as defined therein.

In the case of Cosmetic and Plastic Surgery service any service provided by any person in relation to cosmetic or plastic surgery would be taxable. Here the service receiver and provider can be any person but the service provided should be cosmetic or plastic surgery only. Further surgery due to medical reasons like restore or reconstruct anatomy or functions of body due to congenial defects, etc are excluded.

Similarly on a look at the medical services definition which is proposed to be taxed by the Finance Bill, 2010, one would notice the following:

- a. Service provider – Hospitals, Nursing homes or multi-specialty clinics
- b. Service receiver – employee of business entity or person covered under health insurance scheme.
- c. Service - in relation to health check-up, preventive care or treatment in certain cases
- d. Conditions – Payment for such services to be paid directly by the business entity or insurance company.

Let us examine which of the entities would be covered under the above.

Hospitals

World Health Organization defines the term "hospital" as an institution that provides in-patient accommodation for medical and nursing care. It further elaborates the definition to cover hospitals that assume additional functions- curative, rehabilitative and preventive services- directly or in a consultative capacity, also participating in the training of personnel and in research work.

Nursing Homes

Generally a nursing home would mean a place where patients are treated as inpatients with facilities for admission as inpatients for treatment of illness without or with surgery or conduct of delivery and also includes other gynecological operations where women are received or accommodated for the purpose of sterilisation, hysterectomy, or medical termination of pregnancy etc. with or without overnight inpatient facilities.

Nursing Home would include “any inpatient medical clinic, nursing home, maternity home, hospital, old age homes, day care centers (any intervention which would require observation and on-going care/ monitoring). (Bombay Nursing Home Act (Amendment) 2006

Multi-specialty clinic

A clinic is a medical establishment run by a group of medical specialists meeting for diagnosis of problems and instruction or remedial work in a particular activity, a healthcare facility for outpatient care.

Thus a multi-specialty clinic would be one that would have medical specialists in different branches of medical science.

On an average we can say that less than 10% of the revenue of the hospitals, nursing homes and multi-specialty clinic would fall under the taxable category due to the reason that in India the mediclaim policies and health insurances are opted for mostly as a matter of tax planning and, only for severe diseases treatment is taken at the specified hospitals where the claim would be eligible.

CENVAT Credit Rules, 2004

The 3 very basic definitions that one must be aware of is that of inputs, input services and capital goods defined under the CENVAT Credit Rules, 2004.

A. Inputs is defined in Rule 2(k) of the rules as all goods that are used in or in relation to

- a. manufacture of final products or for any other purpose within the factory of manufacture, or
- b. provision of any output services

with a few exceptions like light diesel oil, high speed diesel oil and motor spirit.

B. Input services is defined in rule 2(l) is any service used

- a. For providing an output service
- b. Directly or indirectly in relation to manufacture of final products and clearance upto place of removal.

and includes all services which would be used for setting up, modernization, renovation, other activities relating to business, advertisement, market research, etc.

C. Capital goods is defined rule 2(a) to contain goods mentioned under certain chapters of the Central Excise Tariff Act, pollution control equipment, components, spares, accessories of such goods, moulds etc. which are used

- a. In the factory of the manufacturer of final goods but does not include any equipment or appliance used in an office, or
- b. For providing output service.

The above 3 definitions are very critical because, if the input tax paid pertains to any of the above 3, only then credit can be taken (subject to certain other conditions).

Conditions for availing credit

The following 4 points would describe the how CENVAT credit can be identified. We will examine only with respect to output services i.e. credits that would be available when taxable services are provided and keep away the discussion pertaining to credits available when taxable goods are sold.

- a. In respect of inputs and input services that are used for providing only taxable services – **FULL credit** can be availed.

An example would be utilization of the services of an air travel agent in respect of the travel of a doctor who is a consultant only for cosmetic or plastic surgery.

- b. In respect of inputs and input services that are used for providing exempt services – **NO credit** can be availed.

An example would be service tax paid on renting of equipment (taxable under supply of tangible goods service) which is used for providing medical services which are not taxed – **NO credit** would be available.

- c. In respect of capital goods, when such goods are used for providing only exempt services – **NO credit** is available. Thus when partly or fully used for providing taxable services then full credit is available.

An example would be purchase of an equipment which would be used for doing cosmetic surgery and for providing exempt services – **FULL credit** available

Another equipment used only for providing medical services that are not taxed – **NO credit** available.

- d. In case of inputs and input services used for providing taxable and exempt services 3 options are available:

- i. Maintain separate records in respect of input and input services used for taxable and exempt services and take credit in respect of those which are used for providing taxable service only.
- ii. Pay 6% on the value of the output services that are exempt.
- iii. Avail credit in proportion of, the turnover of the taxable services provided to the turnover of the total services provided.

Further as an exception to the above is a list of 16 services mentioned in Rule 6(5) in respect of which full credit can be availed if not used exclusively for exempt services. A few of such services are Security agency's service, Banking and Financial services, Management, maintenance or repair service, Commercial or industrial construction service, service of a management or business consultant, architect, interior decorator, etc.

Once the inputs, input services and capital goods are identified and segregated based on whether they are used for providing taxable or exempt or both services then one of the above options that is feasible and beneficial should be chosen and implemented for availing CENVAT credit.

Tax cost incurred by the health industry

Eventhough the health industry was not taxed hitherto they were paying excise duty and service tax on the inputs, capital goods and input services. These have been adding on to their cost. Now with a fraction of their output services being taxed a huge amount of this credit i.e. input / capital goods/input services credit can be availed thus reducing their costs by approximately 3% to 4 %.

Capital Goods: Today technology is playing a very vital role in all areas and the medical industry in no exception to this. A wide variety of state of art equipments are being used by the hospitals and clinics. Many of them are imported as well. On import huge duties are being paid. To list a few of the instruments and appliances that are used in medical, surgical and dental sciences that would eligible for duty credit would be:

- a. Electro cardio-graphs
- b. Ultrasonic scanning apparatus
- c. Echo cardiograph
- d. Cardiac catheters
- e. Ophthalmoscopes
- f. Tonometers
- g. Ophthalmic lasers
- h. Bone saws, drills and trephines
- i. Renal dialysis equipment, blood transfusion apparatus and haemofiltration instruments
- j. Apparatus based on the use of X-rays or alpha, beta or gamma radiations

Input Services:

- a. Proper maintenance of hospitals is of utmost importance and for this a host of services like cleaning service, repair and maintenance services, security agency's service etc. are used on which service tax is paid.
- b. Where an entity is in expansion mode then input services like commercial construction service, works contract service, erection commissioning and installation service would also entitle credit availment which would be of considerable magnitude.

Inputs

Medicines that are purchased from manufacturers or dealers which are used in providing taxable service would qualify as inputs.

Conclusion

Considering the quantum of saving in costs that can be achieved by the health service providers (i.e. hospitals, nursing homes and multi-specialty clinics) proper systems have to be put in place for capturing, segregating and maintaining data relating to the tax liability and CENVAT credit availment and utilization. This should be done before the date of introduction of the levy itself to ensure hassle free implementation and easy availment of the benefits available.

Further whether it would be beneficial to opt for centralized / decentralized registration or to register as an input service distributor has to be analyzed initially itself before the introduction of levy.

Correspondence with the department is another crucial aspect of tax planning and saving of penalty. In this respect it has to be taken care of what information, how and when should be given to the department. Also there are certain correspondences that require to be made with the department statutorily like provisional assessment, correspondence under Rule 6 of the CENVAT Credit Rules, 2004, etc.

Service tax law still being an evolving one it is necessary to get proper professional guidance in the beginning itself to avoid unnecessary harassment by the department and unwanted litigation. For queries post on