Treatment of Accounting Income as taxable Supply and disclosures in financial statements

CA Vinamar Gupta

Accounting Heads

- Discounts/Incentives
- Rental Income from Immovable Property
- Introduction of Asset by partner
- Receipt of Asset on dissolution of partnership firm
- Partners' Salary and Interest
- Directors' Salary
- Foreign Exchange Gain
- Profit on Sale of Assets
- Recovery of Baddebts
- Penalty/Damages/Forfeiture

Discounts /Incentives

Normal Discounts Vs. Excessive Discounts

- Discussion here in is with reference to normal discounts.
- Excess discounts are sometimes imputed to result in “Price being declared not the sole consideration” **[Fiat India Private Limited (Supreme Court) 2012 (283) ELT 161 (SC), where sale below cost continued for 5 years. In this decision “Normal Price” “Price at which goods are ordinarily sold” were weighed by the apex court**
- Though CBEC later clarified that mere selling below manufacturing cost can not be taken sole crieteria to reject transaction value.

Types of Discounts/Incentives

Known before or at the time of supply (resulting reduction of output tax liability of supplier) [It is tax on negative income [SC in Harprasad & Co.] for the supplier impacting his taxable supply under GST. For recipient it is dilemma of non availment/reversal of ITC]

a) Pre Supply: Given before or at the time of supply

b) Post Supply: Established before or at the time of supply but is given post supply

Including:

1. Trade Discount
2. Cash Discount (for prompt payment, known to buyer)
3. Free Samples
4. Buy One get One Free
5. Buy More Save More

Not Known before or at the time of supply (not resulting in reduction of output tax liability for supplier but becomes income/negative expense for recipient impacting his taxable supply)

1. Additional Discounts for undertaking special sales drive, advertisement campaign, exhibition etc.
2. Discounts for Special Price Reduction to Augment Sales
3. Target Incentives
4. Incentives received from Government
5. Volume Discounts without adjustment of GST
6. Discounts/Credit Notes for Warranty Charges passed to Manufacturer
7. Discounts/Credit Notes for Return of Defectives under Warranty arrangement
8. Discounts/Credit Notes for Tour Packages

Pre Supply Discounts

As per section 15(3)(a), pre supply discount get excluded only if following conditions are satisfied:

- Discount is given before or at the time of supply and
- Discount has been duly recorded in the invoice issued in respect of such supply.

Whether discount given recorded in the invoice for subsequent supply shall get excluded?

- From the bare language of the law, answer is no, because condition stipulates recording in the invoice issued in respect of **such supply** only i.e. supply for which discount was given, except where conditions of section 15(3)(b) are satisfied.

For Example Final rates may be revised at the time of final supply with effect from the first supply

SOUTHERN MOTORS 2017 (358) E.L.T. 3 (S.C.)

"…tax invoice or bill of sale ***issued in respect of sales relating to such discount*** shows amount allowed as discount…" - Department insisting on literal interpretation that for discount to be deducted from taxable turnover, it should be mentioned in tax invoice/bill of sale and purchaser reflect in his accounts that he had paid only sum originally charged less discount - *HELD* : ***Reference of discount in tax invoice or bill of sale in first proviso has to be read down in relation to final sale/purchase price and not limited to original sale sans trade discount***

Literal construction - If it results in anomaly or absurdity, courts have to find out underlying intention of legislature and for that purpose, it is within permissible limits strain language so as to avoid unintended mischief. *[para 34]*

What if time of supply and issue of invoice do not match e.g. if discount is not given at the time of advance payment for services but is subsequently recorded in the invoice ?

- As per section 15(3)(a) discount must be imparted before or at the time of supply
- In case of service contracts, if amount is recovered in advance, time of supply is the receipt of amount u/s 13(2) and hence if no discount is allowed or established at the time of advance, no reduction of value of supply shall be allowed.

Post Supply Discounts

As per section 15(3)(b), post supply discount shall get excluded if:

- Such discount is **established** in terms of an agreement entered into at or before the time of such supply and
- Such discount is specifically linked to relevant invoices and
- Input tax credit as is attributable to the discount on the basis of document issued by the supplier has been reversed by the recipient of the supply

It is obvious from the nature of post supply discount that while pre supply discount need to be **given** before or at the time of supply, post supply discount only need to be **established.**

Terms of agreement must establish the discount at the time or before such supply. **Mention of terms on the invoice** or reference to the agreements where in terms are set out may be sufficient compliance.

Recipient of supply need to reverse attributable ITC before the supplier avails such exclusion from the supply.

Reversal of ITC by the recipient **must be based on document issued by the supplier**. It means only if the supplier issues some credit note, only then reversal of ITC by the recipient shall entail exclusion of discount from the supply for the supplier. **Reversal of ITC based on unilateral act of issuing debit note by the recipient might not result in relief sought for by the supplier from the value of supply. It may not even result in allowance of ITC to the supplier**

Mere open ended clause in the agreement without any quantification or criteria is not sufficient to construe post supply discount

AAR Ruling in case of UltraTech Cements 95 taxmann.com 289 dated 27-01-2018, which states that mere a clause in the agreement between supplier and buyer entitling buyer to discount without providing any determinative criteria can not be said to be in compliance to section 15(3)(b)(i) and hence value of supply shall not be reduced in respect of such discount.

It was also added that as the word 'discount' if left open ended or without any qualifications or criteria attached can mean there can be any percentage of discount ranging from bare minimum to even 100 per cent as per discretion of the supplier and certainly such abnormal discounts without any criteria or basis can in no way be considered as fair and at arm's length business transactions and no taxation statute can be construed to be having open ended discount with legislative intent.

Whether recipient compulsorily need to take ITC proportionate to purchases?

- **Circular 122/30/2010-ST dated 30-04-2010** says that As far as the provisions of Rule 4 (7) are concerned, it only provides that the CENVAT credit shall be allowed, on or after the date on which payment is made of the value of the input service and of service tax. The form of payment is not indicated in the same and the rule does not place restriction on payment through debit in the books of accounts. Therefore, **if the service charges as well as the service tax have been paid in any prescribed manner which is entitled to be called 'gross amount charged' then credit should be allowed under said rule 4 (7).** Similar is the position in GST law with reference to S.16(2) 2nd proviso.
- **Circular No. 877/15/2008-CX., dated 17-11-2008:** The entire amount of duty paid by the manufacturer, as shown in the invoice would be available as credit irrespective of the fact that subsequent to clearance of the goods, the price is reduced by way of discount or otherwise. However, if the duty paid is also reduced, along with the reduction in price, the reduced excise duty would only be available as credit. It may, however, be confirmed that the supplier, who has paid duty, has not filed/claimed the refund on account of reduction in price
- **Commissioner Of C. EX., SURAT Versus Trinetra Texturisers Pvt. Ltd. [2004 (166) E.L.T. 384 (Tri. – Mumbai)]**, The suppliers had issued credit notes in favor of the respondents. **Departmental authorities have coerced the respondents to debit the input credit amount equivalent to the duty reduction consequent to value reduction on the inputs,** which occurred consequent to such credit notes. The respondents reverse the corresponding amounts, as directed. The respondent's suo moto took credit for the reversed amount. **Held the entire exercise at the end of the purchaser factory for cutting down the credit, was without the authority of law.** The illegal and coercive reversal of credit on one hand, ***at the same time claiming that the respondents lack the authority to suo moto claim back the said credit, on the other hand, tantamounts to adding insult to injury***. Held that the credit taken was only to restore the actual credit available on the basis of duty paying documents and there was no effort to take credit in excess of the credit mentioned in the duty paying documents

Note: Often ITC is blocked without complying legal provisions. Whether attempt of registered person to take credit in such situations can be thwarted ?

Whether reduction of output tax liability due to credit note can be actually availed ?

- As per **section 49(9),** every person **who has paid the tax** on goods or services or both under this Act shall, unless the contrary is proved by him, be deemed to have passed on the full incidence of such tax to the recipient of such goods or services or both.
- As per **proviso to Section 34(2)**, that no reduction in output tax liability of the supplier shall be permitted, if the incidence of tax and interest on such supply has been passed on to any other person.
- As per **section 54(8)(e)**, Notwithstanding anything contained in sub-section (5), the **refundable amount** shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to the tax and interest, if any, or any other amount paid by the applicant, if he had not passed on the incidence of such tax and interest to any other person.

The Hon'ble High Court of **Punjab and Haryana in the case of *Commissioner of Central Excise, Ludhiana* v. *Bharat Box Factory Ltd*. dated 01-03-2007** has held that **if the credit notes are subsequently issued then burden of duty on the goods would help the assessee to get over the bar of unjust enrichment.**

Supreme Court in ADDISON & CO. LTD 2016 (339) E.L.T. 177 (S.C.)

[Review petition has been dismissed in 2017 (353) ELT A64 (SC). Followed by Supreme Court in *Dharamsi Morarji Chemical Co. Ltd. - 2016 (341) E.L.T.]A154 (S.C.)]*

- The refund claim is on the basis of credit notes raised by the Assessee subsequent to the sale/removal of goods on account of trade discount [Para 25,26]; excess duty paid [Para 31]. The incidence of duty originally paid stood passed on to the buyer. The refund claim was rejected on grounds of unjust enrichment as under:
- S.11B(2)(e) allows refund to buyer, if he had not passed on the incidence of such duty to any other person. Buyer is not restricted to the first buyer from the manufacturer. The buyer mentioned in the above Clause can be a buyer downstream as well.[Para 19]
- If it is not possible to identify the person/persons who have borne the duty, the amount of excise duty collected in excess will remain in the fund which will be utilized for the benefit of the consumers[Para 21]

Comments ; The Supreme Court in **Addison & Co. (supra)** only restricted refund and not reduction of output tax liability because of the provisions under earstwhile law, but the language of section 34(2) proviso restricting reduction of output tax liability also on grounds of unjust enrichment reveals that above judgment can also apply to credit notes where tax incidence has once been borne by the buyer and has passed on to subsequent buyer**. Hence in B2B supplies, reduction of output tax liability u/s 15(2)(b) does not appear to be a hard scenario, except where one has clinching evidence to prove that tax incidence has not been passed on.**

- **Bombay High Court in DAIMLER CHRYSLER INDIA PVT. LTD. 2016 (342) E.L.T. 28 (Bom.)** after considering Addison & Co.(supra) We are of the opinion that if the present assessee relies on the credit notes raised on the dealer, then, an opportunity should be given to it to establish and prove that in pursuance thereof the duty burden which was passed on to the buyer has not eventually fallen on the said buyer on account of this arrangement. Thus, if the dealer has been found to be recovering the amounts or having given credit to the buyer, then, whether the raising of the credit notes would negate the presumption raised in Section 12B of the Act or not is an issue or matter required to be examined by the Tribunal.

Whether credit note can be issued to accommodate the customer who demands invoice on the subsequent date ?

- **TPI ADVISORY SERVICES INDIA P. LTD 2021 (46) G.S.T.L. 136 (Tri. - Bang.):** Assessee paid service tax on services rendered before gst regime. Therafter customers insisted gst invoice. Assessee issued credit note under service tax and issued gst invoice. Assessee demanded refund against credit notes. Assessee pleaded that no tax can be collected without authority of law. Held by Commissioner appeals that issue of GST invoices without supply shall invoke penalty u/s 122(1)(ii). Further held that supplies under service tax were genuine supplies and hence the refund was rejected. Tribunal affirmed the findings of Commissioner appeals.

Forms of Discounts known at the time of supply

Free Samples	Not a supply but ITC to be reversed by the supplier	Circular No. 92/11/2019-GST dated 7-03-2019
Buy One get One Free Need to be applied carefully when tax rate of free items is higher than rate of items charged in the invoice	It is supply of two items for single price. No need to reverse ITC by supplier. Rate of tax shall depend upon whether it is composite or mixed supply	Circular No. 92/11/2019-GST dated 07-03-2019
Buy More Save More Staggered Discounts (Increase in discount with increase in purchase)/Periodic/Year end Discounts	To be excluded from Value of supply	Circular No. 92/11/2019-GST dated 07-03-2019

Discounts not Known before or at the time of supply

As per Circular No. 92/11/2019-GST dated 07-03-2019, Financial/Commercial credit notes for Secondary Discounts (not known at the time of supply), not to be excluded from the value of supply.

Forms:

1. Additional Discounts for undertaking special sales drive, advertisement campaign, exhibition etc.
2. Discounts for Special Price Reduction to Augment Sales
3. Target Incentives
4. Incentives received from Government
5. Volume Discounts without adjustment of GST
6. Discounts/Credit Notes for Warranty Charges passed to Manufacturer
7. Discounts/Credit Notes for Return of Defectives under Warranty arrangement
8. Discounts/Credit Notes for Tour Packages

Availability of ITC to the buyer of goods on secondary discount allowed by the supplier

MRF (AAR Tamilnadu) dated 22/01/2019 103 taxmann.com 278

It was held in this case that ITC is not available to the buyer dealer on the amount of discount enjoyed by him because to that extent consideration has not been paid by him which **disentitles the proportionate ITC** as per Rule 37 read with Section 16(2) 2nd Proviso.

As per **Circular 105/24/2019-GST dated 28-06-2019** withdrawn by Circular No. 112/31/2019 dated 03-10-2019, dealer will not be required to reverse ITC attributable to the tax already paid on such post-sale discount received by him through issuance of financial / commercial credit notes by the supplier of goods in view of the provisions contained in second proviso to sub-rule (1) of rule 37 of the CGST Rules read with second proviso to sub-section (2) of section 16 of the CGST Act as long as the dealer pays the value of the supply as reduced after adjusting the amount of post-sale discount in terms of financial / commercial credit notes received by him from the supplier of goods plus the amount of original tax charged by the supplier.

2nd Proviso to Rule 37:

Provided further that the value of supplies on account of any amount added in accordance with the provisions of **clause (b) of sub-section (2) of section 15 shall be deemed to have been paid** for the purposes of the second proviso to sub-section (2) of section 16.] **(Inserted vide notification No. 26/2018-Central Tax, dated 13.06.2018**

Section 15(2)(b)

The value of supply shall include any amount that the supplier is liable to pay in relation to such supply but which has been incurred by the recipient of the supply and not included in the price actually paid or payable for the goods or services or both

Comments:

Circular intends to say that amount of discount is required to be borne by the supplier of goods but is incurred by the recipient by forsaking the payment by the supplier.

Additional Discounts for undertaking special sales drive, advertisement campaign, exhibition etc.

- **As per Circular 105/24/2019-GST dated 28-06-2019 withdrawn by Circular No. 112/31/2019 dated 03-10-2019**, if the additional discount given by the supplier of goods to the dealer is the post-sale incentive requiring the dealer to do some act like undertaking special sales drive, advertisement campaign, exhibition etc., **then such transaction would be a separate transaction and the additional discount will be the consideration for undertaking such activity and therefore would be in relation to supply of service by dealer to the supplier of goods**. The dealer, being supplier of services, would be required to charge applicable GST on the value of such additional discount and the supplier of goods, being recipient of services, will be eligible to claim input tax credit (hereinafter referred to as the "ITC") of the GST so charged by the dealer.

PHILIPS INDIA LTD 1997 (91) E.L.T. 540 (S.C.)

- It seems to us clear that the advertisement which the dealer was required to make at its own cost benefited in equal degree the appellant and the dealer and that for this reason the cost of such advertisement was borne half and half by the appellant and the dealer. Making a deduction out of the trade discount on this account was, therefore, uncalled for. As to the after sales service that the dealer was required under the agreement to provide, it did of course enhance in the eyes of intending purchasers the value of the appellant's product, but such enhancement of value enured not only for the benefit of the appellant; and earn a larger profit. The guarantee attached to the appellanit also enured for the benefit of the dealer for, by reason thereof, the dealer got to sell more it's products specified that they could be repaired during the guarantee period by the appellant's dealers anywhere in the country. Thus, though one dealer might have to repair goods sold by another dealer and incur costs in that regard, he also had the benefit of having the goods he sold reparable throughout the country. The provision as to after sales service, therefore, benefited not only the appellant; it was a provision of mutual benefit to the appellant and the dealer, therefore the reduction of trade discount of 2% is uncalled for. [paras 5, 6, 8]

Mumbai Tribunal in ALEMBIC GLASS INDUSTRIES LTD. 2001 (135) E.L.T. 1230 (Tri. - Mumbai) distinguished Philips India where entire entire expenditure was incurred by the dealer only but was overruled by Supreme Court in Almbic Glass Insustries' own case before the apex court

Special Discount to augment Sale

- As per **Circular 105/24/2019-GST dated 28-06-2019 withdrawn by Circular No. 112/31/2019 dated 03-10-2019**, if the additional discount is given by the supplier of goods to the dealer to offer a special reduced price by the dealer to the customer to augment the sales volume, then such additional discount would represent the consideration flowing from the supplier of goods to the dealer for the supply made by dealer to the customer. This additional discount as consideration, payable by any person (supplier of goods in this case) would be liable to be added to the consideration payable by the customer, for the purpose of arriving value of supply, in the hands of the dealer, under section 15 of the CGST Act. ***The customer, if registered, would be eligible to claim ITC of the tax charged by the dealer only to the extent of the tax paid by the said customer to the dealer in view of second proviso to sub-section (2) of section 16 of the CGST Act.***

AS per definition of Consideration u/s 2(31) also payment made in money or otherwise by the recipient **or any other person** gets taxed. Hence amount received by discount i.e. payment made otherwise than in money from supplier of goods instead of customer (i.e. payment received from a person than buyer) appears to be getting taxed, irrespective of the withdrawal of the Circular No.105.

Further as per section 15(2)(e), the value of supply shall include **subsidies directly linked to the price** excluding subsidies provided by the Central Government and the* State Governments.

This also leads to further implication that while the goods may be exempt or may be taxed at different rate the amount of discount may get taxed 18%. **From accounting angle if there is loss in trading account without taking into account rebate and discount, it will invite taxman to poke his nose into taxpayer's affairs.**

Santosh Distributors [2019] 110 taxmann.com 496 (AAR - KERALA) dated 16-09-2019

Without drawing any reference from Circular No. 105 , the ruling lays down that:

- Discount offered to the customer reimbursed by the registered person's supplier shall be added to the value of supply made by the registered person
- Customer shall however be entitled to ITC only to the extent of tax charged
- Financial credit note issued by supplier shall not entail any proportionate reduction of ITC
- AAR ruling also states that reimbursed amount shall be added to value of supply to the customer. Hence the reimbursed amount shall be taxable as goods and not as service as per AAR Ruling.

Incentives

The Federal Court of Australia in AP Group Ford agreed with its dealers to pay certain sums of money to dealers which achieved monthly and quarterly sales targets that Ford set based on the dealer's size and past performance. **Targets were based on the number of cars sold to eligible customers in the qualifying period, not the value of the cars sold**. Once a car was sold and delivered to an eligible customer the details would be entered into the vehicle information system and, in about the middle of the following month, based on the information so entered Ford would issue the dealer with a tax invoice for the incentive payment plus 10% GST and shortly thereafter pay that amount to the dealer.

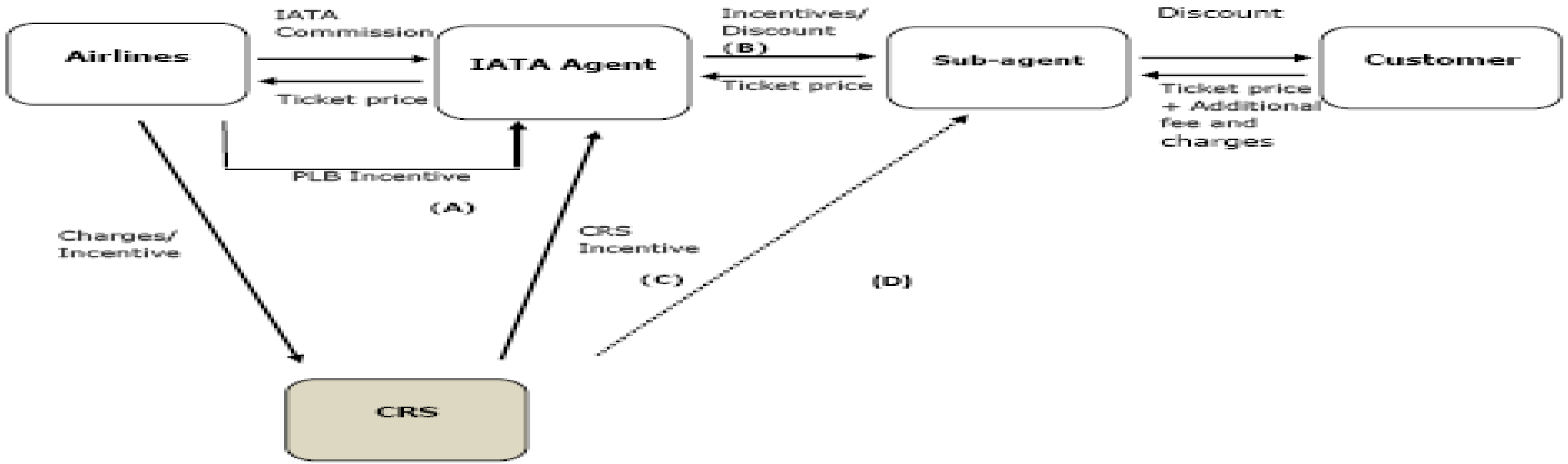
- On analysis, the so-called supplies for consideration identified by the Commissioner are **nothing more than the encouragement of an overall business relationship between the manufacture and the dealer to the mutual benefit of both**. The relationship involves a whole raft of obligation from one to the other all, presumably, with the **ultimate objective of maximizing their respective commercial positions**. As the AP Group put it, the overall relationship contemplates a continuing dialogue between wholesaler and retailer in which promises are routinely exchanged, **but to characterize this dialogue as involving supply after supply is unrealistic and impractical**. To characterize the payment of the incentives intended to encourage the overall relationship to operate efficiently as involving supplies for consideration equally unpersuasive. **A dealer will always wish to sell as many cars as practicable and to move old stock to make way for new stock. So too a dealer will always wish its ordering arrangements to be the most efficient and economically beneficial to it. The manufacture will have the same objectives**. It is this context which underpins the Tribunal's conclusion that the payments are not for the supply of anything by the dealer. As the Tribunal said at the dealer (which must be inferred to act in an economically rational manner in the ordinary course) will always want to run the business in this way. **The fact that the dealer receives a payment as an incentive when certain thresholds associated with running the business in this way does not mean that the dealer is supplying a service to the manufacturer for consideration. If the incentive payment were not available there is no basis to infer that the dealer would not behave in the same way for free**. For these reasons there cannot be said to be any supply for consideration in these arrangements.

Incentives

Air Travel Industry:

The travel industry basically comprises of five key players namely

1. Airlines,
2. Travel agents,
3. Central Reservation System Companies,
4. Sub-agents and
5. Passengers



A perusal of the aforesaid chart would show that for sale of tickets, the IATA agents, apart from the commission that they receive from the airlines, also receive Performance Linked Bonus, which is linked to guaranteed booking of a minimum number of airline tickets. This incentive is indicated at A in the aforesaid chart. In certain cases, the sub-agents also book airlines tickets through IATA agent and where sub-agents achieve a pre-determined target on booking through a particular IATA agent, the IATA agent also pays an incentive to the sub-agents. This incentive is indicated at B in the aforesaid chart. The CRS Companies also allow IATA agents to subscribe to their portal for booking tickets for the passengers/sub-agents. **Earlier, the IATA agents were charged by the CRS Companies for access to their portal but due to increasing competition in the market, the CRS Companies stopped charging the agents and instead, in order to increase the flow of business, started to part with a portion of the commission paid to them by airlines to the IATA agents when the agents achieve a minimum quantum of bookings through the concerned CRS portal**. These incentives are indicated at C and D in the aforesaid chart.

Kafila Hospitality & Travels (P.) Ltd(New Delhi Cestat) 18-3-21 2021 (47) G.S.T.L. 140 (Tri. - LB)

- For booking a ticket, a travel agent would require a system to book the tickets. **A travel agent is free to choose any CRS system. A passenger would never request a travel agent to book his ticket only through Amadeus/Galileo/Abacus system**. Can it, therefore, be said that the travel agent is engaged in the promotion of a particular CRS system.[Para 61]. **Mere selection of software or exercising of a choice would not result in any promotional activity. The Department has not pointed out at any 'activity' undertaken by an air travel agent that promotes the business of the CRS Company.[Para 65].** The passenger cannot be deemed to be an audience for promotion of the business of CRS Companies, for the passenger can neither book directly through a CRS Company nor can a passenger be influenced by any travel agent to book through a particular CRS Company.[Para 67]
- The air travel agent is, by sale of airlines ticket, ensuring the promotion of its own business even though this may lead to incidental promotion of the business of the airlines/CRS Companies.[Para 71]
- Consideration, which is taxable under section 67 of the Finance Act, **should be transaction specific**. Incentives, on the other hand, are based on general performance of the service provider and are not to related to any particular transaction of service. It needs to be noted that commission, on the other hand, is dependent on each booking and not on the target. If the air travel agent does not achieve the pre-determined target, incentives will not be paid to the travel agents.[Para 77]
- Incentives paid for achieving targets cannot termed as "consideration"[Para 80]

Car Dealers

- Tribunal in **Rohan Motors Limited v. Commissioner of Central Excise, Dehradun 2020 (12) TMI 1014 - CESTAT NEW DELHI**, the Tribunal held that incentives are not leviable to service tax. The relevant paragraph is reproduced below :-
- 9. The first issue that arises for consideration is whether service tax would be leviable on incentives prior to July, 2012.
- 10. As noticed above, the appellant purchases vehicles from MUL and sells the same to the buyers. It is clear from the agreement that the appellant works on a principal to principal basis and not as an agent of MUL. This is for the reason that the agreement itself provides that the appellant has to undertake certain sales promotion activities as well. **The carrying out of such activities by the appellant is for the mutual benefit of the business of the appellant as well as the business of MUL. The amount of incentives received on such account cannot, therefore, be treated as consideration for any service. The incentives received by the appellant cannot, therefore, be leviable to service tax.**

Incentives received from Government

As per section 15(2)(e), The value of supply shall include—subsidies directly linked to the price excluding subsidies provided by the Central Government and the* State Governments.

SECRETARY, MINISTRY OF COMMERCE Vs Vinod and Company 2019 (367) E.L.T. 881 (S.C.)

The objects of the policy are essentially to stimulate industrial growth by providing easy access to imported capital goods, raw materials and components, to substitute imports and promote self-reliance and to provide an impetus to exports by improving the quality of incentives. The Exim policy is an incident of the fiscal policy of the State and of its overall control over foreign trade. As an incident of its policy, the State may provide a regime of incentives. The provision of those incentives does not render the State a service provider or the person who avails of the incentives as a potential user of any service. The State, in exercise of its authority to utilise and collect revenue, puts in place diverse regulatory regimes under the law. The regime may provide for modalities for compliance, penalties for breach and incentives to achieve the purpose of the policy. The grant of these incentives does not constitute the State as a service provider

Volume Discounts without adjustment of GST

Volume Discounts received on Purchases without adjustment of GST

KWALITY MOBIKES (P) LTD. 2019 (30) G.S.T.L. 668 (A.A.R. - GST)

- The Applicant when makes more purchases is eligible for the volume discount on purchases and a credit note is issued by the authorised supplier and no adjustment of price is made in respect of the goods already sold nor any adjustment of GST is made in the credit note. The Applicant is also not claiming any reduction in input tax credit already claimed by him as it does not affect the price of the goods sold. Hence, the amount received by the Applicant is in the form of an incentive provided by the authorised supplier and does not affect the sale price of the goods already sold and hence there is no liability to charge GST on the same.

Volume Discount received on Retail (on sales) in the form of credit note without any adjustment of GST

KWALITY MOBIKES (P) LTD. 2019 (30) G.S.T.L. 668 (A.A.R. - GST)

Applicant when sells more than his target is eligible for the incentive which is provided by the authorised supplier in the form of a credit note without affecting the sale price of the goods purchased or sold. Even this is in the form of incentive and no adjustment of price nor tax is done either by the Applicant or the authorised supplier. Hence, the amount received by the Applicant is in the form of an incentive provided by the authorised supplier and does not affect the sale price of the goods already sold and hence there is no liability to charge GST on the same

Since the credit note is issued as a post-sale event, the same is not covered under the clause (a) of the above provision. Further, the Applicant has not reversed the input tax credit attributable to the discount received in the form of credit note from the authorised supplier, the same cannot be covered under clause (b) above. Hence in view of the above, the credit note issued by the supplier in the pertinent case does not have any effect on the value of supply and hence is only a financial document for account adjustment for the incentive provided. Hence there is no effect on the GST.

Warranty Charges passed on to Manufacturer

CITY MOTORS 2019 (28) G.S.T.L. 286 (Tri. - Chennai)

- Passport Bonus Card Scheme - Authorised dealer collecting amounts under ‘Passport Bonus Card Scheme’ on behalf of manufacturer of motor vehicles for servicing and benefits after warranty period - Dealer merely acting as agent and passing on amounts collected to manufacturer without retaining any money - No commission or incentive paid to such dealer - Service Tax not liable on money so collected - Section 65(19) of Finance Act, 1994.

Discounts/Credit Notes for Return of Defectives under Warranty arrangement

- Credit notes can be issued for return of goods resulting reduction of output tax till September of next year. Post September there is no reduction of output tax liability in the hands of supplier, but issue of credit note might result in accrual of tax liability in the hands of recipient.
- Held by Supreme Court **in Mohd. Ekram Khan & Sons on 21-07-2004**, that transaction is taxable sale **because in a case manufacturer may have purchased from the open market parts for the purpose of replacement of the defective parts. For such transactions, it would have paid taxes.** The position is not different because the assessee had supplied the parts and had received the price.

Held by Supreme Court in ***TATA MOTORS LTD. 2019 (25) G.S.T.L. 481 (S.C.)***

- The judgment in the *Mohd. Ekram Khan & Sons* case (supra) refers to the credit notes received as consideration for the replacement; but it is a moot point whether credit notes can be treated as a mode of payment or not. ***We have some reservations in respect of the observations and legal propositions laid down in the Mohd. Ekram Khan & Sons case (supra) and consider it appropriate that the matter be considered by a larger Bench***

Discounts/Credit Notes for Tour Packages

MERINO INDUSTRIES LTD 2020 (37) G.S.T.L. 209 (Tri. - All.)

I have carefully gone through the submissions from both the sides and perused the records. I have also gone through the ruling by Hon'ble Gujarat High Court in the case of *Gujarat State Fertilizers & Chemicals Ltd.* (supra). I note that Hon'ble Gujarat High Court in the said case had examined the particular agreement and it was clear that as per the said agreement the agents were appointed as stockiest. I note that in the present case the tour packages were arranged for dealers. I further note that this Tribunal in the case of *M/s. Simbhaoli Sugar Ltd.* (supra) have held that if commission is paid to sales commission agent for effecting sale of goods manufactured by the assessee then service tax paid on such commission would be available as input service credit to the manufacturer. I note that **it was possible for the appellant to pay in cash expenses for tour. Instead they have provided them tour packages. Therefore, the said tour packages can be considered as dealer's commission.** Therefore, Cenvat credit of service tax paid on tour packages are admissible as Cenvat credit in the present case.[Para 5]

Rental Income of residential dwelling for use as residence

- Service by way of renting of residential dwelling for use as residence" is exempt under Entry 13 of NN 12/2017 but Supply of Hotel accomodation i.e. *supply, by way of accommodation in hotels, inns, guest houses, clubs, campsites or other commercial places* ***meant for residential or lodging purposes*** *including the supply of time share usage rights by way of accommodation [as defined in Para 4(*xxxiv*) of 11/2017] is taxable*
- Lease of property comprising 73 rooms to company engaged in commercial activity of renting of rooms for dwelling and providing boarding and hospitality services held not for residential dwelling having regard to number of rooms and facilities provided **[Lakshmi Tulasi Quality Fuels [2020] 117 taxmann.com 942 (AAR - ANDHRA PRADESH) MAY 5, 2020]**
- Renting of residential complex to a company providing units to students for residence on long term basis is not renting of residential dwelling units but "hotel" and is not exempt [Taghar Vasudeva Ambrish [2020] 116 taxmann.com 373 (AAR - KARNATAKA) 23-03-2020]

- *The issue is what is difference between "residential dwelling" and "accommodation in hotels, inns, guest houses, clubs, campsites or other commercial places meant for residential purposes" ?*

- *Residential Dwelling is defined* ***in Para 4.13.1of Educational Guide*** *under service tax regime as under:*

"The phrase 'residential dwelling' has not been defined in the Act. It has therefore to be interpreted in terms of the normal trade parlance as per which it is any residential accommodation, **but does not include hotel, motel, inn, guest house, camp–site, lodge, house boat, or like places meant for temporary stay"**

- Hence "residential dwelling" and "accomodation in hotel, *nns, guest houses, clubs, campsites" are mutually exclusive.*
- However the only difference which is brought out by the above definition is that "residential dwelling" is not **meant for** temporary stay while "hotel,inn, guest house, club, campsite" **are meant for temporary stay**
- **Hence actual stay in residential dwelling may be short while stay in hotel may be long but it is not the actual use but "meant for" use which demarcates the difference between residential dwelling on one side and hotel, guest house on other side**.

Held by **Supreme Court in Associated Hotels of India Ltd vs RN Kapoor:**

".....It is sufficient to state that in its ordinary connotation the word 'hotel' means a house **for entertaining strangers or travellers**: a place where lodging is furnished to transient guests as well as one where both lodging and food or other amenities are furnished.....

A hotel in common parlance means a place where a proprietor makes it his business to furnish food or lodging, or both to travellers or other persons. **A building cannot be run as a hotel unless services necessary for the comfortable stay of lodgers and boarders are maintained**. Services so maintained. vary with the standard of the hotel and the class of persons to which it caters; but the amenities must have relation to the hotel business. Provisions for heating or lighting, supply of hot water, sanitary arrangements, sleeping facilities, and such others are some of the amenities a hotel offers to its constituents....."

Hence hotels have transient guests and travellers and services necessary for comfortable stay of lodger and boarders are maintained.

- **Another way of looking at the difference can be that in case of residential dwelling services for comfortable stay are not maintained but may be made available only on specific request, however in case of hotels these services are invariably maintained though the guest may opt not to avail such services.**

Additional guidance provided by Educational Guide is: Whether residential accomodation is or is not exempt can be decided as under

1	2
If.....	**Then.....**
(i) a residential house taken on rent is used only or predominantly for commercial or non-residential use.	the renting transaction is not covered in this negative list entry.
(ii) if a house is given on rent and the same is used as a hotel or a lodge	the renting transaction is not covered in this negative list entry because the person taking it on rent is using it for a commercial purpose.
(iii) rooms in a hotel or a lodge are let out whether or not for temporary stay	the renting transaction is not covered in this negative list entry because a hotel or a lodge is not a residential dwelling.
(iv) government department allots houses to its employees and charges a license fee	such service would be covered in the negative list entry relating to services provided by government and hence non- taxable.
(v) furnished flats given on rent for temporary stay (a few days)	such renting as residential dwelling for the bonafide use of a person or his family for a reasonable period shall be residential use; but if the same is given for a short stay for different persons over a period of time the same would be liable to tax.

What is Per Unit Per day in the context of Hotel, Hostel and Villa ?

Per Unit Per day value of accommodation services decides the gst rate. If per unit per day value is less than Rs. 1000, gst is exempt, if per unit per day value is above Rs.1000 but less than Rs. 7500, gst is 12% and if it is more than Rs. 7500, gst is 18%.

But what is per unit per day in the context of Hotel, Hostel and Villa discussed in **Isprava Hospitality (AAR Maharashtra) on 17-03-2020*** as under :

1. **Hotel** : per day per unit = Hotel room and can not be on the basis of beds or occupancy [*Bombay High Court in Mandovi Hotels*]

2. Hostel: per day per unit= Bed [*AAR Chattisgarh in Kamal Kishore Agarwal Ramnath Bhimsen Charitable Trust*]

3. **Villa** : Per day per Unit = Entire Villa, where charge is made for entire villa and not on per room basis and at one point of time only one customer is entitled to take Villa on lease.

- Hence pettern of renting shall decide what is per day per unit.

Introduction of Asset into Partnership

Sunil Siddharthbhai 156 ITR 509 (SC) 27-09-1985 [before Section 45(3) which was introduced by Finance Act 1987 and specifically taxed the introduction of capital asset in partnership firm in the hands of partner]

1. Whether Transfer: Yes, by way of **reduction of the exclusive interest in the totality of rights of the original owner into a joint or shared interest with other persons. An exclusive interest in property is a larger interest than a share in that property. To the extent to which the exclusive interest is reduced to a shared interest it would seem that there is a transfer of interest. Therefore, when a partner brings in his personal asset into the capital of the partnership firm as his contribution to its capital, he reduces his exclusive rights in the asset to shared rights in it with the other partners of the firm. [Para 11]**
2. **What is consideration received by the partner : The credit entry made in the partner's capital account in the books of the partnership firm does not represent the true value of the consideration**. It is a notional value only, intended to be taken into account at the time of determining the value of the partner's share in the net partnership assets on the date of dissolution or on his retirement, a share which will depend upon a deduction of the liabilities and prior charges existing on the date of dissolution or retirement It is not possible to predicate beforehand what will be the position in terms of monetary value of a partner's share on that date.

Consideration for transfer of asset by partner = Right to share profit during subsistence + Share in partnership assets after reducing liabilities on disssolution. This value can not be predicted in monetary terms on the date of entering into partnership, hence OMV under Rule 27 may be taken.

Receipt of asset on dissolution of partnership Firm

- **Quoted in para 12 of Sunil Siddharthbhai 156 ITR 509 (SC) 27-09-1985:**

It has been held by this Court in *CIT* v. *Dewas Cine Corporation* [1968] 68 ITR 240, *CIT* v. *Bankey Lal Vaidya* [1971] 79 ITR 594 and recently in *Malabar Fisheries Co.* v. *CIT* [1979] 120 ITR 49 as well as by the Punjab and Haryana High Court in *Key Engg. Co.* v. *CIT* [1971] 82 ITR 950, the Kerala High Court in *CIT* v. *Nataraj Motor Service* [1972] 86 ITR 109 and the Gujarat High Court in *CIT* v. *Mohanbhai Pamabhai* [1973] 91 ITR 393 that when a partner retires or the partnership is dissolved, what the partner receives is his share in the partnership. What is contemplated here is a share of the partner *qua* the net assets of the partnership firm. On evaluation, that share in a particular case may be realised by the receipt of only one of all the assets**. What happens here is that a shared interest in all the assets of the firm is replaced by an exclusive interest in an asset of equal value. That is why it has been held that there is no transfer. It is the realisation of a pre-existing right**.

Partners' Salary and Interest

Cadila Healthcare Limited [2021] 127 taxmann.com 112 (Ahmedabad - CESTAT) 27-04-2021

In partnership firm M/s Zydus Healthcare , there are two partners namely Cadila Healthcare Staff Welfare Trust and German Remedies Ltd. In addendum of the partnership agreement, appellant **(Cadilla) agreed to provide certain services to firm partnership M/s Zydus Healthcare related to promotion and marketing of firm's product and various related services**. The appellant towards the said services received remuneration from M/s Zydus Healthcare on which they have paid the service tax. Subsequently, when they realised on the basis of their consultant's advice that the services provided by a partner to a partnership firm does not fall under the ambit of services as per Finance Act, 1994, they had filed for refund claims.

Held by Cestat:

The appellant has carried out the activities which were assigned to the appellant by the partnership firm in the capacity of the partner. These activities were not undertaken pursuant to a separate and independent contract for provision of services between the appellant of the partnership firm. Therefore, the activities carried out by the appellant for its partnership firm is part of its duties as a partner. In this arrangement, it cannot be said that the partner is a service provider and partnership firm is service recipient. Partners and partnership firm cannot be treated as two distinct persons.[Para 4]

R.M. Chidambram Pillai (Supreme Court) :'Firm' is a collective noun. a compendious expression to designate an entity, not a person. since a contract of employment requires two distinct persons, viz., the employer and the employee, there cannot be a contract of service, in strict law, between a firm and one of its partners. So that any agreement for remuneration of a partner for taking part in the conduct of the business must be regarded as portion of the profits being made over as a reward for the human capital brought in.

Punjab and Haryana High Court in Bhagwant Singh vs Commissioner of Income Tax 1959 PH Air 59; When a partnership agreement recites that one of the partners will receive a salary for the services rendered by him to the partnership business the contract is regarded as a contract of partnership and is not designated as a contract of service.

Supreme Court in the case of Chandrakant Manilal Shah; Just like a cash asset, the mental and physical capacity generated by the skill and labour of an individual is possessed by or is a possession of such individual. Indeed, skill and labour are by themselves possessions. "Any possession" is one of the dictionary meanings of the word 'property'. In its wider connotation, therefore, the mental and physical capacity generated by skill and labour of an individual and indeed the skill and labour by themselves would be the property of the individual possessing them. They are certainly assets of that individual and there seems to be no reason why they cannot be contributed as a consideration for earning profit in the business of a partnership firm

Directors' Salary

Circular No: 140/10/2020 - GST dated 10-06-2020

- It is clarified that the part of Director‟s remuneration which are declared as „Salaries‟ in the books of a company and subjected to TDS under Section 192 of the IT Act, are not taxable being consideration for services by an employee to the employer in the course of or in relation to his employment in terms of Schedule III of the CGST Act, 2017
- It is further clarified that the part of employee Director‟s remuneration which is declared separately other than „salaries‟ in the Company‟s accounts and subjected to TDS under Section 194J of the IT Act as Fees for professional or Technical Services shall be treated as consideration for providing services which are outside the scope of Schedule III of the CGST Act, and is therefore, taxable. Further, in terms of notification No. 13/2017 – Central Tax (Rate) dated 28.06.2017, the recipient of the said services i.e. the Company, is liable to discharge the applicable GST on it on reverse charge basis

Circular No. 115/9/2009-S.T., dated 31-7-2009 by CBEC

- When companies making payments to their Managing Directors/Directors (Whole-time or Independent) terming them as "Commission". Even if it is termed as commission will not be termed as commission within the scope of Business Auxiliary Services hence no service tax leviable on that.
- The Managing Director/Directors (Whole-time or Independent) are part Board of Directors and discharge management functions and are not into consultancy or advisory to the company. The payments made by Companies, to Directors cannot be termed as payments for providing management consultancy service. Therefore, it is clarified that the amount paid to Directors (Whole-time or Independent) is not chargeable to service tax under the category 'Management Consultancy service'. However, in case such directors provide any advice or consultancy to the company, for which they are being compensated separately, such service would become chargeable to service tax.

CESTAT judgment was in the case of Allied Blenders And Distillers (P.) Ltd. [2019] 101 taxmann.com 462 (Mumbai - CESTAT) CESTAT, MUMBAI BENCH.

- Here the bench held "Where assessee-company paid remuneration to its four whole time Directors for managing day-to-day affairs of company and made necessary deductions on account of Provident fund, Professional Tax and TDS as applicable and declared these Directors to all statutory authorities as employees of company, remuneration paid to Directors was nothing but salary and assessee was not required to discharge service tax on remuneration paid to Directors"

Foreign Exchange Gains and Losses

- *Rule 34:* **Rate of exchange of currency, other than Indian rupees, for determination of value.**
- *(1) The rate of exchange for determination of value of taxable goods shall be the applicable rate of exchange as notified by the Board under section 14 of the Customs Act, 1962 for the date of time of supply of such goods in terms of section 12 of the Act.*
- *(2) The rate of exchange for determination of value of taxable services shall be the applicable rate of exchange determined as per the generally accepted accounting principles for the date of time of supply of such services in terms of section 13 of the Act*
- **When goods or services are exported out of India**

a) Goods: Rate of Exchange shall be as per date of issue of invoice on or before date of removal of goods. Services: For service time of supply is 30 days from provision of service

- However as per AS-11., Foreign currency transactions must be recorded, **on initial recognition** in reporting currency, by applying the exchange rate between the foreign currency and the reporting currency to the foreign currency amount **at the date of the transaction. Further** at the end of financial year all the foreign currency monetary items must be reported at the closing rate
- Hence for goods both services due to difference in time of supply and date of transaction (when risks and rewards of ownership are transferred/date of provision of service/proportionate completion), closing rate etc valuation differences are bound to occur
- **When services are imported**
- Time of supply is payment date generally. Hence generally there should not be difference because ultimately transaction in AS-11 is recognized at its settlement rates of monetary items

Profit on Sale of Assets

1. Whether margin scheme is applicable to capital goods on which ITC has not been taken?

A person can not be said to be “dealer in” Capital goods. Hence irrespective of the fact that no ITC has been availed on purchase of capital goods, Rule 32(5) shall not apply.

2. Old and Used Vehicle: Where ITC has not been taken NN 8/2018 shall apply on difference between sale price and Purchase price/wdv.

3. As per **section 33**, **the amount of tax which forms part of the price at which such supply is made is required to be reflected in tax invoice**. However it also implies that if the tax does not form part of the price, then tax amount need not be indicated in the invoice. Hence tax need to be mentioned only when it is part of price. The seller may opt to pay tax on margin excluding the amount of tax. This shall result in his tax liability being marginally higher as compared to tax liability calculated as per Rule 35.

4. Capital goods on which ITC has been taken to be dealt as per Section 18(6) read with Rule 42. E.g. Asset Value is Rs. 100000. ITC @ 18% =Rs.18000, purchased on 1-1-21, Sold for Rs. 50000 @ 18%;Output Tax= Rs.9000, on 31-01-2021. ITC to be reversed = 18000-20% [5% x4]= Rs. 14400. Tax to be paid is Rs. 14400

- Capital Goods on which ITC has not been taken or Pre GST capital goods to be taxed at transaction value
- Transfer of Business : Entry 2 of 12/2017
- Cessation of Business:

➢ Schedule I Para 1 : Applicable only where ITC has been taken. Not applicable to pre GST Assets.

➢ Applicability of Para 4© of Schedule II to pre GST assets

Recovery of Baddebts

- As per Section 7(1)(a) of the CGST Act, 2017 the presence of consideration is must for any transaction to be regarded as supply (except for 4 situations covered under Schedule-I of the CGST Act).
- In cases where the debts recoverable by supplier are written off as bad debts , there will be no flow of consideration to such supplier, rather in such cases the amount recoverable is written off from books. Therefore, writing off of bad debts would not be treated as an independent supply and thus will not be subjected to GST.
- Similarly at the time of recovery there is no flow of goods or services from the supplier

Penalty/Damages/Forfeiture

Chennai Cestat in Steel Authority of India Ltd. On 26-07-2021:

- The amount recovered by assesse as liquidated damages for late delivery of goods by the suppler. Also earnest money forfeited from the customers not making payment till date specified in sale order. Ground rent recovered on per lot on every day basis, for extension of due date for making payment. The department treated the same as consideration for agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act and taxed the amount received.
- Held by **Chennai Cestat in Steel Authority of India Ltd. On 26-07-2021** quoting Delhi Cestat on South Eastern Coalfields Ltd. and affirming M.P. Poorva Kshetra Vidyut Vitran (Delhi Cestat) that it is trite that an agreement has to be read as a whole so as to gather the intention of the parties. **The intention of the parties certainly was not for flouting the terms of the agreement so that the penal clauses get attracted. The penal clauses are in the nature of providing a safeguard to the commercial interest of the appellant and it cannot, by any stretch of imagination, be said that recovering any sum by invoking the penalty clauses is the reason behind the execution of the contract for an agreed consideration It is not the intention of the appellant to impose any penalty upon the other party nor is it the intention of the other party to get penalized.**
- Hence the amount received was held not taxable.

Disclosures in the financial Statements

1. Discount has been allowed in the normal course of business and no extraordinary discount has been allowed.
2. In respect of credit notes Incidence of tax has not been passed on to any other person.
3. Advertisement expenditure has been incurred and reimbursed for mutual benefit of dealer and manufacturer
4. Incentives received are not in respect of services rendered to the supplier.
5. Rent is being received in respect of property meant for residential dwelling
6. No Input tax credit has been claimed on the vehicle sold.
7. No tax has is included in the price recovered for the sale of vehicle
8. Penalties/Damages have been stipulated/recovered only to safeguard the commercial interest of the entity and not under any agreement to refrain from doing an act
9. Recovery of baddebts is against the debts already written off
10. Foreign Exchange gains and losses are on account of application of AS-11.
11. TDS u/s 192 has been paid on Directors' Salary.


Thank
you