

Vasai Branch of WIRC of ICAI
Seminar dated 28.8.2010 on
“Issues in VAT and Service Tax related
to Construction Industry”

C. B. THAKAR
B.Com., LLB, F.C.A.
Advocate

Aspects of VAT with relation to Immovable Property and Construction Contracts - An Update

(1) INTRODUCTION

In relation to immovable properties, the first thing, which comes to our mind, is whether sale of immovable property attracts any sales tax? Under Sales Tax Laws the tax is leviable only on sale of 'goods'. As per Sales Tax Laws, only moveable goods are considered to be goods. Therefore immovable properties of any nature cannot fall in the Sales Tax net. Therefore, sale of flats/shops etc. cannot be subject matter of Sales Tax. This is uncontroverted position and hence not dealt with further. However, whether any particular transaction is for sale of immovable property or is a transaction of sale of moveable goods may become debatable.

Such issues mainly arise when along with immovable property certain movable goods in fixed condition are also disposed of. For example, while disposing of Factory building there may also be disposal of machinery fixed in it. An attempt may be made by Sales Tax authorities to say that to the extent of machinery, there is sale. However this cannot be correct in all cases. It depends upon nature of machinery installed. The situation can be seen from two angles. If along with immovable property any movable goods passes, but without separate consideration, then in such cases it can very well be said that since consideration is not bifurcated nor possible to be bifurcated, there is no sale of such moveable goods and hence no taxable event arises.

The other angle is that the moveable goods are fixed in the building and there is no intention to sever the same before transfer of immovable property. For example, the machinery is sold in fixed condition and there is no intention to sever them. In such cases, even if values of factory building and machineries are shown separately, it can very well be argued that there

is sale of immovable property only and not of machinery, as there is no intention to deliver machinery separately as moveable goods. A reference can be made amongst others, to judgments of Maharashtra Sales Tax Tribunal in case of **Lyods Steel Ind. (S.A.2091 of 98 dt.23.3.2001)**, **Herdelia Chemicals Ltd. (S.A. 1826 of 1999 dt.31.10.2001)**, **Basawraj Printing Press (S.A.525 of 86 dt.30.11.87)**, **Libra Leather Ind. Ltd. (S.A.479 & 480 of 1988 dt.30.9.89)**, **Paramount Sintors Ltd.(S.A.1220 of 1995 dt.20.4.2002)** and **Pepsico India Holdings P. Ltd. (S.A.1074 of 2001 dt.19.06.2002)** etc.

However if the facts turns out to be otherwise, i.e., there are separate values as well as intention to sever items is evident, then the transaction to the extent of moveable goods can be considered as amounting to sale. A reference can be made to judgment in case of **Indoswe Engg. Co.(S.A.1357 of 98 dt.18.11.2000)**.

Similar different situations can also arise in relation to Works Contract theory and transfer of immovable property depending upon facts of each case. A reference can be made to judgment of M.S.T. Tribunal in case of **Sukhkarta Apartments (S.A.29 to 32 of 1996 dt.6.7.2002)**.

In this case appellant was arguing that the activity is not covered by the then Maharashtra Works Contract Act since there is sale of immovable property, being sale of constructed houses. Tribunal found that the agreement for sale of land and construction of building were separate, and therefore, though it was argued that it is sale of immovable property, a constructed house, Tribunal held that the construction part is liable to Works Contract, being separate construction contract.

A reference is also required to be made to the important judgment of Supreme Court in **K. Raheja Construction (141 STC 298)**. In this case the developer, constructing building, but selling the flats etc. before completion of construction (sale under Construction), is held liable to Works Contract Tax. Though the judgment is under Karnataka Act, it will have repercussions in Maharashtra also. This aspect is discussed later.

In contrast a case can be considered where it was a composite contract for providing land with constructed tenements.

In determination order in case of **M/s.Rehab Housing Pvt. Ltd.. & Larsen & Toubro Ltd.(JV) (WC-2003/ DDQ-11/Adm-12/B-276 dt.28.6.2004)**, the Commissioner of Sales Tax Maharashtra State has held that the transaction is composite one i.e. providing land with constructed tenements and hence it is not covered by Sales Tax Provisions including Works Contract Act.

Thus, though in normal case it can be said that immovable properties are not subject matter of Sales Tax, in light of above stated contingencies it is necessary to see the implications of Sales Tax Laws on particular facts of the case. In case of sale of flats/ shops or bungalows etc. the issue of sales tax will not arise. However when the agreements are not so simple but involve two components like land and construction or a issue arise whether particular property is immovable property or not, more attention is required to be given to above aspects of Sales Tax. From 20.6.2006, the MVAT Act provides for definition of works contract, which is inserted in section 2(24). The said definition reads as under.

“(24) “sale” means a sale of goods made within the State for cash or deferred payment or other valuable consideration but does not include a mortgage, hypothecation, charge or pledge; and the words “sell”, “buy” and “purchase”, with all their grammatical variations and cognate expressions, shall be construed accordingly;

***Explanation.*— For the purposes of this clause,-**

(a) a sale within the State includes a sale determined to be inside the State in accordance with the principles formulated in section 4 of the Central Sales Tax Act, 1956 (74 of 1956);

(b) (i) the transfer of property in any goods, otherwise than in pursuance of a contract, for cash, deferred payment or other valuable consideration;

(ii) the transfer of property in goods whether as goods or in some other form involved in the execution of a works contract including, an 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 commissioning of any movable or immovable property ----“

However inspite of above definition there will not be any change in the legal position discussed above. Unless there are separate contracts for land and construction no tax liability can be attracted.

Having above preliminary observations about sales tax on immovable properties, to my mind the more integrated issues in relation to immovable properties will arise in relation to bringing into existence the immovable properties. The discussion in this paper is restricted to issues of Works Contract Tax under Maharashtra Value Added Tax Act,2002 (VAT Act). In other words, the sales tax issues involved in relation to construction of immovable properties and construction industry are dealt with here. A brief study on above lines can be as under.

(2) POSSIBLE SITUATIONS OF WORKS CONTRACT TAX IN RELATION TO IMMOVABLE PROPERTIES AND CONSTRUCTION INDUSTRY

Normally immovable properties mean the properties of the nature of buildings etc.. It can also include the factory buildings in which machinery etc. are embedded in it. In fact, the issue whether a property is moveable or immovable, depends upon various factors, like nature of construction, intention of parties and other relevant factors. The attempt here is not to discuss nature of movable/immovable properties as such. For this paper the discussion is restricted to contracts of construction of buildings etc. with relation to Works Contract under VAT Act. In this respect following situations can be discussed.

(i) Self construction of property

Under this situation normally a builder will develop property on his own plot. He will purchase the building materials and will construct the same. Here no question of Works Contract Tax arises since it is one's own development and no element of transfer of property in goods to other party is involved. Normally the sale will be of ready flats etc., i.e., immovable property and hence not liable to any tax. But if there is sale of any 'moveable' items like sale of discarded items etc., to that extent, liability under VAT Act can arise. Here the issue is again required to be seen in light of judgment in case of **K. Raheja Construction(cited supra)**. The above judgment pertained mainly to Developer and its full implications are

discussed later. However in this judgment the Supreme Court has observed that even if one is not developer but constructing on his own land, still in given circumstances he can be liable to tax. In other words, a dealer constructing buildings on his own land but entering into agreement for sale of flats etc. before completion of construction, can be liable to tax under VAT Act. This aspect is to be seen along with the issues discussed subsequently in relation to developer.

A point about issue of 'C' forms for purchase of building materials from other states in above situation, can be considered here. As builder may be getting registered under VAT Act he can also get himself registered under CST Act and hence will become entitled to issue of 'C' forms against his purchases. However it may be remembered that when the builder is purchasing the materials for his own construction he cannot be entitled to purchase materials against 'C' forms. When he purchases materials for construction of building etc. the intension is to effect sale of ready flats etc.. Surely the materials so purchased against 'C' forms cannot be said to be for purpose of resale or for use in manufacturing of goods for sale etc.. There is no resale or such use in manufacturing etc., when materials are used in construction and therefore such use is not fulfilling condition of permissible uses in 'C' form. Therefore, purchases against 'C' form is not allowable to builder under above circumstances. However if the construction is one which is liable to VAT (as in case of K. Raheja) than 'C' form can be issued.

(ii) Construction on land belonging to other on the basis of

Development agreement

Under this type, normally a builder will enter into agreement for development of land belonging to other party. It will be joint development agreement. It is assumed here that the construction is not for landlord but by joint development. Builder will be constructing a building for sale of flats/shops. The flats/shops may be sold to prospective customers when the construction is on. As averred above the construction is not for landlord but on joint development basis. Secondly even though prospective customers book the flats/shops etc. the intention is to give them possession of flats/shops as immovable property. The construction activity itself cannot be

said to have been started because of any agreement from customer. Thus this activity also does not attract any Works Contract liability. The above issue is well settled by various determination orders passed by the Commissioner of Sales Tax. A reference can be made to order in the case of **Unity Developer & Paranjape Builders (DDQ 1188/ C/40/ Adm-12 dt.10.3.88)**.

K. Raheja effect

However change, if any, is required to be noted by judgment of Supreme Court in **K. Raheja Construction (141 STC 298)** in relation to above issue. The brief history of Works Contract taxation is already given earlier. However the definition of 'works contract' is not given in the Constitution. Therefore its meaning is left to be understood by the respective parties.

In certain Legislations like, Karnataka Sales Tax Act, the definition of 'Works Contract' is given while in Maharashtra Sales Tax on Transfer of property in execution of Works Contract (Re-enacted) Act,1989 no such definition was given. In Maharashtra Value Added Tax Act,2002 such definition is provided from 20.6.2006, which is reproduced earlier.

In above Supreme Court case the controversy before Supreme Court was about the meaning of 'works contract'. The Honorable Supreme Court has laid down a law which will have far reaching effects upon the builders and developers in entire India.

The facts in above case are that M/s. K. Raheja entered into an agreement with land owner for development of the land with construction of residential and commercial buildings. Pursuant to development agreement, M/s.K.Raheja also entered into agreements with its customers for sale of flats/shops. The terms included to handover the possession of flats/shops. The value of land and construction was shown separately. The assessing authorities in Karnataka levied sales tax on the said transactions, considering the agreements as 'sale' by way of Works Contract within the meaning of Karnataka Act. The definition of 'Works Contract' in Karnataka Act read as under:

“‘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 and commissioning of any movable or immovable property.”

The argument of assessee was that the construction was on his own property (because of development agreement with land owner) and the buyer is to take possession of flat/office. It was further argued that there is, therefore, no transfer of property in goods in execution of works contract, since a owner of land property cannot execute agreement for transfer of building materials while constructing on his own land. Therefore it was submitted that the sale was of flat and offices, i.e. immovable property, not liable to sales tax.

Supreme Court, however, negated above submission.

Supreme Court, relying upon the above given definition, held that the scope is wider than normal meaning of Works Contract and includes the contracts entered into while the flat/office is under construction. Supreme Court observed that constructing building on one's own land (but shown as sold separately in agreement) does not make any difference. Supreme Court further clarified that if the agreement is for sale of flats etc., after the construction is complete, then of course, it will not attract any sales tax as it will be a sale of immovable property. Therefore the above law declared by Supreme Court will bring the developers/ builders within the purview of sales tax liability if the facts are similar. To the extent of agreements entered into before Construction of flats or offices is complete, the liability as works contract can arise.

In Maharashtra, as mentioned earlier the Commissioner of Sales Tax has taken a view that in case of developers/builders constructing buildings and entering into agreements before construction is complete, there is no sales tax liability under Works Contract Act. However now the situation may change. Upto 19.6.2006 Works Contract was not defined under the MVAT Act. From 20.6.2006 the term is defined as reproduced earlier. The effect of K. Raheja is to be seen in light of this development and if facts are similar to facts in case of K. Raheja liability can arise. As per Supreme Court, entering into agreement before the construction is complete, amounts to deemed sale, by way of transfer of property in goods in the execution of Works

Contract. However it has to be kept in mind that the above judgment can apply, where the value of land and construction is separately mentioned and agreed upon. This position also gets supported from judgment of Gauhati High Court in case of **Magus Construction P. Ltd. v. Union of India (15 VST 17) (Gauhati)**, wherein the judgment in **K. Rahaja** is distinguished. In majority cases in Maharashtra composite values are shown. Therefore its applicability will be limited to the cases where land value and construction is shown separately.

In the Budget Speech of Finance Minister delivered on 19.3.2008 in the Assembly it was mentioned that a deduction for land price in a Construction Contract will be provided to find out taxable price. Accordingly Government has prescribed Rule 58(1A). The short analysis of above rule 58(1A) is as under:

Rule 58 (1A) – Brief Analysis of Rule

Vide Notification dtd. 01.06.2009, the Government of Maharashtra has inserted Rule-58(1A) in the MVAT Rules, 2005. The said rule is introduced for granting deduction for cost of land from total contract value. The said rule is reproduced below for ready reference.

“(1A) In case of a construction contract, where alongwith the immovable property, the land or, as the case may be, interest in the land, underlying the immovable property is to be conveyed, and the property in the goods (whether as goods or in some other form) involved in the execution of the construction contract is also transferred to the purchaser such transfer is liable to tax under this rule. The value of the said goods at the time of the transfer shall be calculated after making the deductions under sub-rule(1) and the cost of the land from the total agreement value.

The cost of the land shall be determined in accordance with the guidelines appended to the Annual Statement of Rates prepared under the provisions of the Bombay Stamp (Determination of True Market Value of Property) Rules, 1995, as applicable on the 1st January of the year in which the agreement to sell the property is registered.

Provided that, deduction towards cost of land under this sub-rule shall not exceed 70% of the agreement value.”

The back ground of this rule is that, in light of judgment of Supreme Court in case of **Raheja Development Corporation (141 STC 298)** the

government understands that under construction contracts are liable to tax under MVAT as works contracts. Accordingly, definition of works contract is also inserted in the Act from 20.06.2006. In light of above understanding the government has thought it fit to grant deduction for cost of land, so that ultimately the tax is attracted on value of materials used in the contract.

However the above understanding of government is subject to further litigation. The judgment in **Raheja Development Corporation (141 STC 298)** itself is referred to Larger Bench by Supreme Court in case of **Larsen & Toubro Limited and another Vs. State of Karnataka and another. (17 VST 460)**. The amendment in MVAT Act, 2002 contemplating tax on under construction contracts is also challenged before Bombay High Court.

However, pending the litigation, the government has provided above rule to give deduction for cost of land from contract value. The analysis of above rule give rise to following issues.

- a) The rule is to apply in case of construction contract, where the conveyance of land or interest in land (immovable property) is contemplated in such contract, alongwith transfer of property in goods involved in such contract. In short, the rule is stated to apply where both, immovable property as well as movable property are involved.

Though rule contemplates as above, the legality of such position is not free from doubt. There appears to be no power to bifurcate contract value into immovable property and others, when the value of contract is composite. In other words, the state government has no power to notionally divide composite contract involving immovable property and movable property. The power as available under Article 366 (29A)(b) in respect of works contract is lacking in case of contract involving immovable property. As such legality of this rule can be challenged before proper forum.

- b) The rule contemplates to grant deduction for immovable property, when the said property is to be conveyed. Whether the conveyance of the property is to be to the contractee itself or anybody else is also not clear. For example, in case of agreement for sale of flat, when the construction is under progress, (under construction agreements for sale of flat) a possibility can arise that such contract will be covered by this rule. The flat value will include cost of

land also. However, the land will not be conveyed to the flat purchaser but it may be conveyed to the society which may be formed in future. The question arises whether contractor will get any deduction in above circumstances.

The issue requires clarification.

- c) The rule contemplates to determine the value of the land as per guidelines appended to the annual statement of the rates prepared under provisions of Bombay Stamps (Determination of True Market Value of Property) Rules, 1995, as applicable on 1st January of the year, in which the agreement to sell the property is registered. This will also create difficulties. The agreement may be entered in one year but may be registered in subsequent year/years. The liability for works contract may arise on entering the agreement. The question is how to decide the value in the year of agreement itself. The further guidelines are required.
- d) The rule says to take the deduction under this rule i.e. 58(1A) as well as, as per rule 58(1). Rule 58(1) is regarding deduction for labour charges from contract value. A question may arise whether rule 58(1) should be applied after taking deduction under 58(1A) or both should be applied simultaneously. From plain reading it appears that deduction should be claimed simultaneously from the total contract value.

In fact, there are several issues concerning rule 58(1A). The above is indicative list of few issues.

Section 42(3A)

The broad issues about liability on builders are already discussed above. Vide amendment effected on 1.5.2010, section 42(3A) has been inserted in MVAT Act,2002 effective from 1.4.2010. By this section powers are given to the Government to notify composition scheme for builders. It can be noted that the new scheme of composition is not a levy section. It is only one more method of discharging liability. Therefore, the core issue whether builder, on the given facts, is liable to tax or not is to be seen in light of legal position discussed above. If the builder considers himself liable to tax then in addition to the other methods he can now discharge liability by way of this new composition scheme.

1% Composition Scheme for Builders & Developers

Certain Important aspects of the above Notification can be noted as under:

- a) The Scheme is notified by Notification dated 9.7.2010 issued under 42(3A). The scheme applies to Builders/Developers, who undertake the construction of flats etc., wherein they also transfer land or interest underlying the land. Normally, Builders/Developers commence construction on their own land as per their own project planning. The land is to be transferred to the society or association which may be formed by the buyers of the premises collectively, after possession is given. An issue may arise that there will not be transfer of land or interest in land to any individual purchaser with whom agreements are entered into. In case of flats/premises, each sale agreement can be considered to be construction contract. Therefore, if one reads the Notification literally then it may be said that when the land or interest in land is not transferred to the very individual purchaser, the notification can not apply. Therefore, to avoid any dispute in future, the department is required to clarify about nature of transfer of land or interest in land, wherein it may be clarified that transfer to society etc., will also be eligible for the Composition Scheme.
- b) The Scheme can apply to registered dealers only. It is possible that in view of debatable position, the Builders/Developers are not registered under MVAT Act, 2002. However, if they wish to take benefit of this Scheme at this moment or any time in future, it is necessary that they remain registered dealer. However, being registered it doesn't mean that the Builder is accepting the liability. He can be registered dealer but can still show no turnover in the returns, considering his contracts as contracts for immovable property. In future, if the liability accrues because of clarity in the legal position, he can opt for this Scheme. Though one of the conditions mention that the dealer should include the contract price in the return in which the agreement is registered and pay the tax on it by declaring such contract price as turnover, this can be done even by revising the return at appropriate time. Therefore, at present, awaiting clarity of the law, builder can file return without declaring turnover of such contracts.

It can also be noted that if the Builder applies today for registration, his earlier transactions from 20.06.2006 onwards will also be scrutinized for levy of liability. This new Composition Scheme does not bring new tax but it only provides one more method for discharging liability effective from 01.04.2010. Assuming that Builder opts for this Composition Scheme from 01.04.2010, he can contest the liability for past period, if the issue arises.

- c) The Scheme is applicable to agreements registered after 01.04.2010. Therefore, even if the agreement is executed earlier but registered after 01.04.2010, it will be eligible.
- d) The Composition money is 1% of the agreement amount, specified in the agreement or value adopted for the purpose of stamp duty, whichever is higher. The condition also debars set off on the purchases. The further conditions also debar such dealer from effecting purchases against 'C' forms, as well as debars from issuing form no. 409 to the sub-contractors. The further conditions also mention that the dealer will not be entitled to change the method of computation of tax liability. From the plain reading, it appears that this condition is to be seen qua each contract and not project as a whole. The last condition mentions that the dealer under this Composition Scheme should not issue tax invoice. The issue may arise as to whether Builder can collect 1% composition separately. Though, the provisions relating to tax invoice are not worded happily, from the clarification issued by the Commissioner of Sales Tax, it can be said that though tax invoice cannot be issued, still in the normal invoice or bill etc., the Builder can charge composition amount separately. Otherwise he has to include in the agreement price.

From the overall scenario, it appears that though there is uncertainty about attraction of sales tax liability on under construction contracts, the Builders/Developers may consider the risk factor and may pass on the burden to the prospective purchasers. This will result in burden upon the common person. The issue will be more aggravating, if ultimately the liability is not upheld by the judicial forum. There will be number of difficulties in getting back the tax which was not due to the government. The earliest clarification of legal position is the need of the day.

Development on Barter Basis

In certain construction transactions the builder/developer is liable to construct premises for land owner for allowing development right etc.. The issue is, whether the builder (developer) is liable to pay tax on such transaction. For example X allows Y to develop on his land. In consideration thereof Y is under obligation to handover specific number of premises to X without any receipt of money from X i.e. free. The issue is whether any liability under VAT law arises in such case. Thus the main issue in such case is about liability, if any, as works contract in relation to handing over of premises to X. The concerned land belongs to X. Y will be constructing building on X's land using his building materials etc. in relation to premises handed over to X. There is thus transfer of property from Y to X. In normal course this transaction would have amounted to taxable works contract and liable to tax. However in this case the situation is peculiar.

As per Sales Tax Laws to be a taxable sale transaction under Sales Tax Laws it is necessary that the consideration is in money terms.

The legal position in this regard can be elaborated, briefly as under.

The term 'sale' is defined as under in section 2(24) of MVAT Act,2002 as under:

"(24) "sale" means a sale of goods made within the State for cash or deferred payment or other valuable consideration but does not include a mortgage, hypothecation, charge or pledge; and the words "sell", "buy" and "purchase", with all their grammatical variations and cognate expressions, shall be construed accordingly;...."

Thus, the transaction to be a sale, it should be a sale of goods for cash, deferred payment or other valuable consideration. Unless money consideration is agreed upon, there is no question of 'sale' as per Sales Tax Laws.

The situation can further be scrutinized from the definition of 'sale price' in section 2(25) of MVAT Act,2002, which reads as under.

"(25) "sale price" means the amount of valuable consideration paid or payable to a dealer for any sale made including any sum charged for anything done by the seller in respect of the goods at the time of or

before delivery thereof, other than the cost of insurance for transit or of installation, when such cost is separately charged.----"

(underlining ours)

Thus it is the amount agreed for transfer of property which is sale price and which can be subjected to tax. Unless the valuable consideration is available in money terms no tax can be calculated as the tax is always in % of the sale price.

The combined reading of above two definitions amply shows that unless the transfer of goods to other party is against money consideration there is no 'sale' transaction for the purpose of MVAT Act and no tax can be levied on such transaction. Though above position is clear from the above cited provisions, we can make reference to some decided cases for further clarification.

M/s.Gannon Dunkerley & Co. (9 STC 353)(SC)

Supreme Court while dealing with the taxability of transaction of works contract under the sales tax laws, observed about the ingredients of 'sale' as under on page 365 of 9 STC.

"Thus, according to the law both of England and of India, in order to constitute a sale it is necessary that there should be an agreement between the parties for the purpose of transferring title to goods, which of course presupposes capacity to contract, that it must be supported by money consideration, and that as a result of the transaction property must actually pass in the goodsSo also if the consideration for the transfer was not money, but other valuable consideration, it may then be exchange or barter but not a sale. And if under the contract of sale, title to the goods has not passed, then there is an agreement to sell and not a completed sale."

Thus from above passage it is clear that to be a 'sale' following criteria should be fulfilled.

- (i) There should be two parties to contract i.e. seller/purchaser,
- (ii) The subject matter of sale is moveable goods,
- (iii) There must be money consideration and

(iv) Transfer of property i.e. transfer of ownership from seller to purchaser.

Thus it is clear that there should be consideration against the transfer of ownership in goods.

The consideration has to be in money terms. If the consideration is not in money terms but in any other mode it may be case of barter or exchange but not 'sale'.

C.I.T. v. Motors & General Stores (P) Ltd. (66 ITR 692)

In this respect reference can be made to the Supreme Court judgment in case of **C.I.T. v. Motors & General Stores (P) Ltd. 66 ITR 692**. In this case, Supreme Court has observed as under on page 695/696 of 66 ITR: "Section 54 of the Transfer of Property Act defines 'sale' as a transfer of ownership in exchange for a price paid or promised or part paid and part promised. Section 54 of the Transfer of Property Act reads as follows: "sale' is a transfer of ownership in exchange for a price paid or promised or part paid and part promised"

There is no definition of the words 'price' in this Act. But it is well settled that the word 'price' is used in the same sense in this section as in section 4 of the Sales of Goods Act, 1930 (Act III of 1930) (see the decisions of a full Bench of the Madras High Court in Madam Pillai v. Badrakali Ammal) Section 4 of the Sale of Goods Act reads as follows:

- (1) A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price. There may be a contract of sale between one part owner and another.
- (2) A contract of sale may be absolute or conditional.
- (3) Where under a contract of sale the property in the goods is transferred from the seller to the buyer, the contract is called a sale, but where the transfer of the property in the goods is to take place at a future time or subject to some condition thereafter to be fulfilled, the contract is called an agreement to sell.

(4)An agreement to sell becomes a sale, when the time elapses or the conditions are fulfilled subject to which the property in the goods is to be transferred.”

Section 2(10) of the Sale of Goods Act defines ‘price’ as meaning the money consideration for a sale of goods. The presence of money consideration is therefore an essential element in a transaction of sale. If the consideration is not money but some other valuable consideration it may be an exchange or barter but not a sale.”

(underlining ours).

M/s.Davi Dass Gopal Krishnan and Others (22 STC 430)(SC)

In this case the issue arose as to whether ‘other valuable consideration’ will include consideration other than money. Hon.Supreme Court has observed as under on page 444/445:

“Bearing that in mind let us look at clause (ff) in section 2 of the principal Act in which the said clause was inserted. The ingredients of the definition of ‘purchase’ are as follows: (i) there shall be acquisitions of goods; (ii) the acquisition shall be for cash or deferred payment or other valuable consideration; (iii)the said valuable consideration shall not be other than under a mortgage, hypothecation, charge or pledge. Clause (h) of section 2 defines ‘sale’ thus:

‘sale’ means any transfer of property in goods other than goods specified in Schedule C for cash or deferred payment or other valuable consideration but does not include a mortgage, hypothecation, charge or pledge.

If we turn to the Sale of Goods Act, section 4 thereof defines a contract of sale of goods. It reads:

“A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property in goods to the buyer for a price...”

The essential requisites of sale are (i) there shall be a transfer of property or agreement to transfer property by one party to another; and (ii) it shall be for consideration of money payment or promise thereof by the buyer.

...

Now, coming to the expression 'price', it is no doubt defined in the Sale of Goods as 'money consideration'. Cash or deferred payment in clause (ff) of section 2 of the Act satisfies the said definition. The expression 'valuable consideration' has a wider connotation, but the said expression is also used in the same collocation in the definition of 'sale' in section 2(h) of the Act. The said expression must bear the same meaning in clause (ff) and clause (h) of section 2 of the Act. It may also be noticed that in most of the sales tax acts the same three expressions are used. It has never be argued or decided that the said expression means other than monetary consideration. This consistent legislative practices cannot be ignored. The expression 'valuable consideration' takes colour from the preceding expression 'cash or deferred payment'. If so, it can only mean some other monetary payment in the nature of cash or deferred payment. We, therefore, hold that clause (ff) of section 2 of the Act is not void for legislative incompetence."

(underlining ours)

Thus "other valuable consideration" used in definition reproduced above will have the meaning as consideration in money terms only and not any other consideration.

M/s.Radhas Printers v. State of Kerala (90 STC 201) (Kerala)

In this judgment also applying the law laid down by Hon.Supreme Court in Devi Dass Gopal Krishnan, the Kerala High Court has held as under on page 205/206:

"11.These decisions therefore cannot be treated to hold that 'other valuable consideration' could be goods or other property and that consideration need not be money consideration. In the decisions in Sales Tax Commissioner v. Ram Kumar Agarwal (1967) 19 STC 400, the Allahabad High Court held that 'other valuable consideration' which occurs in section 2(h) of the U.P. Sales Tax Act,1948, must be interpreted on the basis of the rule of ejusdem generis to mean cheques, bills of exchange or such other negotiable instruments and that they cannot cover a case where no price is paid. The Supreme Court in the decision in Devi Dasss

Gopal Krishnan v. State of Punjab (1967) 20 STC 430 held that the expression 'valuable consideration' takes colour from the preceding expression cash or deferred payment. Thus to constitute 'sale' within the meaning of the KDST Act, the same should be for consideration either in cash or deferred payment, or other valuable consideration; and other valuable consideration in the context must be interpreted to mean cheques, bills of exchanges or any such negotiable instruments."

(underlining ours)

Thus the legal position is more than clear that unless the transfer of property by the seller to buyer is against money consideration there cannot be 'sale' transaction for the purposes of sale tax laws.

In above example of X, the consideration is in form of allowing development. It is not in money terms. It is transaction of barter but not transaction of sale by way of works contract. Therefore the transaction between Y and X is not a taxable Works Contract under Sales Tax Laws and no liability as Works Contract is attracted.

(iii) Construction Contractor

The normal position which we come across day to day is that a developer/builder gets the work of construction completed through the contractor. He may award the whole construction work to one contractor or may divide the work and award different works to different contractors. For example, he may appoint one contractor for whole construction or may appoint different contractors for different works, like for construction, for electrical fittings etc..

However in all these cases the contractor will be the person who will be liable to discharge tax liability. As a contractee or employer, builder will not be liable to any Works Contract Tax. There is no concept of unregistered dealer purchases under VAT Act and hence whether the contractor is registered or not, no liability on builder can arise as purchases from URD etc.

It may also be noted that if builder himself purchases the goods and gives contract for labour portion only, then there is no question of any liability under VAT Act. Thus the liability, if any, is to be seen in light of

above facts. Even if the purchases are from unregistered dealers, still there will not be any liability on such purchases under VAT Act as there is no concept of levy of purchase tax.

In fact under above category many different situations can arise depending upon the facts of each case. The facts of each agreement are to be considered carefully to see whether the contract is covered by VAT Act or not and accordingly the liability, if any, be decided.

In this respect it can further be noted that if builder gives the contract liable under VAT Act to contractor, then his liability can be only upto the extent of Deduction of Tax on contract and payment of same to Government. As stated above there is no direct burden of tax on him. The indirect tax burden will fall on builder, as contractor will pass on his burden to the builder and hence builder should be aware of the provisions of VAT Act to estimate and seek ways for minimizing the tax burden. The various situations of discharging Works Contract tax under VAT Act are discussed below which can be considered for estimating the liability.

Similarly the TDS provisions under VAT Act are also discussed below which should be kept in mind.

Discharging tax liability under MVAT Act,2002

Following are five ways of discharging tax liability under MVAT Act,2002. This will apply to construction contractor as well as other Works Contractors also.

(i) If in the contract itself the value of the goods and labour is shown separately, then such values of goods will be taxable at appropriate rates. In this respect reference can be made to judgment in case of **Imagic Creative P. Ltd. (12 VST 371)(SC)**, where such division is upheld by Supreme Court.

If the values are not separately mentioned but only one value is specified, then the contractor can discharge liability by any of modes discussed below.

(ii) As per Statutory Provisions

Under this system the tax payable on value of goods can be arrived at by adopting Rule 58 of VAT Rules,2005. The Rule 58(1) is as under:

“58. (1) The value of the goods at the time of the transfer of property in the goods (whether as goods or in some other form) involved in the execution of a works contract may be determined by effecting the following deductions from the value of the entire contract, in so far as the amounts relating to the deduction pertain to the said works contract:--

- (a) labour and service charges for the execution of the works;
- (b) amounts paid by way of price for sub-contract , if any, to sub-contractors ;
- (c) charges for planning, designing and architect’s fees;
- (d) charges for obtaining on hire or otherwise, machinery and tools for the execution of the works contract;
- (e) cost of consumables such as water, electricity, fuel used in the execution of works contract, the property in which is not transferred in the course of execution of the works contract;
- (f) cost of establishment of the contractor to the extent to which it is relatable to supply of the said labour and services;
- (g) other similar expenses relatable to the said supply of labour and services, where the labour and services are subsequent to th1e said transfer of property;
- (h) profit earned by the contractor to the extent it is relatable to the supply of said labour and services: -----“

In the alternative, i.e. if dealer cannot ascertain the labour portion on its own as per above, dealer can adopt the standard deduction given in Table in Rule 58(1). The said table is as under.

“Table

Serial No.	Type of Works contract	*Amount to be deducted from the contract price (expressed as a percentage of the contract price)
(1)	(2)	(3)
1	Installation of plant and machinery	Fifteen per cent.
2	Installation of air conditioners and air coolers	Ten per cent.
3	Installation of elevators (lifts) and escalators	Fifteen per cent.

4	Fixing of marble slabs, polished granite stones and tiles (other than mosaic tiles)	Twenty five per cent.
5	Civil works like construction of buildings, bridges, roads, etc.	Thirty per cent.
6	Construction of railway coaches on under carriages supplied by Railways	Thirty per cent.
7	Ship and boat building including construction of barges, ferries, tugs, trawlers and dragger	Twenty per cent.
8	Fixing of sanitary fittings for plumbing, drainage and the like	Fifteen per cent.
9	Painting and polishing	Twenty per cent.
10	Construction of bodies of motor vehicles and construction of trucks	Twenty per cent.
11	Laying of pipes	Twenty per cent.
12	Tyre re-treading	Forty per cent.
13	Dyeing and printing of textiles	Forty per cent.
14	Annual maintenance contracts	Forty per cent
15	Any other works contract	Twenty five per cent

*Note : The percentage is to be applied after first deducting from the total contract price, the quantum of price on which tax is paid by the sub-contractor, if any, and the quantum of tax separately charged by the contractor if the contract provides for separate charging of tax.

(2) The value of goods so arrived at under sub-rule(1) shall, for the purposes of levy of tax, be the sale price or, as the case may be, the purchase price relating to the transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract.”

It can be seen that as per Rule 58(1) main provision, contractor can determine his own labour portion and take deduction of the same from gross

contract value. The balance will be liable to tax. The said taxable portion is to be divided between 0%, 4%/5% and 12.5% goods and tax be worked out accordingly.

(iii) In the alternative, i.e. if contractor cannot ascertain the labour portion on his own, he can adopt the standard deduction given in Table. The portion remaining after given deduction will be liable to tax at applicable rates i.e. 0%, 4%/5% and 12.5%.

It may also be mentioned that if one follows any of above methods, he can avail full set off on goods purchased under VAT from local RD, subject to other conditions of set off.

Composition Schemes

(iv) In the alternative contractor can pay tax by Composition Scheme and in that case, he will be required to pay tax on full contract value @ 8%. No deduction of labour charges etc. will be available. If one pays tax as per above composition scheme, he will be entitled to set off @ 64% of the normal set off otherwise available. The reduction will apply to the goods which get transferred and not to other goods. In other words, for those goods full set off will be available.

(v) One more method of composition is available in case of Notified Construction Contracts. The list of notified construction contract is as under.

“FINANCE DEPARTMENT

Mantralaya, Mumbai 400 032, dated the 30th November 2006

NOTIFICATION

The Maharashtra Value Added Tax Act, 2002.

No VAT.1506/CR-134/Taxation-1-- In exercise of the powers conferred by clause (i) of the **Explanation** to sub-section (3) of section 42 of the Maharashtra Value Added Tax Act, 2002 [Mah. IX of 2005], the Government of Maharashtra hereby notifies the following works contracts to be the 'Construction Contracts' for the purposes of the said sub-section, namely :-

(A) Contracts for construction of,--

(1) Buildings,

- (2) Roads,
- (3) Runways,
- (4) Bridges, Railway overbridges,
- (5) Dams,
- (6) Tunnels,
- (7) Canals,
- (8) Barrages,
- (9) Diversions,
- (10) Rail tracks,
- (11) Causeways, Subways, Spillways,
- (12) Water supply schemes,
- (13) Sewerage works,
- (14) Drainage,
- (15) Swimming pools,
- (16) Water Purification plants and
- (17) Jettys

(B) Any works contract incidental or ancillary to the contracts mentioned in paragraph (A) above, if such work contracts are awarded and executed before the completion of the said contracts.

By order and in the name of the Governor of Maharashtra. ”

If contract is covered by above list then dealer can discharge liability by paying 5% on total contract value. If dealer pays by this composition scheme then set off on purchases will be granted after reduction @ 4% of purchase price.

(vi) 1% Composition scheme for builders.

The details of this scheme are already discussed above and hence not repeated here.

Dealer may adopt any of the modes suitable in its case and contract wise choice can also be made.

It can also be mentioned that the choice of method can be made per contract.

TDS provisions

As stated above the Builder /Developer will be liable to comply TDS provisions wherever applicable. The short gist of TDS provisions is given below for ready reference.

- i) Section 31 of the MVAT Act authorized the Commissioner of Sales Tax to bring suitable TDS scheme in respect of Works Contract or any purchase transaction. However at present the scheme is made applicable in respect of works contract transaction only.
- ii) By Notification dated 29.8.2005, the Commissioner of Sales Tax has specified the list of employers liable to TDS and the rates of TDS.
- iii) The list of employers liable for deduction of TDS is as under:

SCHEDULE

Serial No.	Classes of Employers	Amount to be deducted
(1)	(2)	(3)
(1)	The Central Government and any State Government,	Two per cent of the amount payable as above in the case of a contractor who is a registered dealer and four per cent in any other case.
(2)	All Industrial, Commercial or Trading undertakings, Companies or Corporations of the Central Government or of any State Government, whether set up under any special law or not, and a Port Trust set up under the Major Ports Act, 1963,	-- do --
(3)	A Company registered under the Companies Act, 1956,	-- do --
(4)	A local authority, including a Municipal Corporation, Municipal Council, Zilla Parishad, and Cantonment Board,	-- do --
(5)	A Co-operative Society excluding a Co-operative Housing Society registered under the Maharashtra Co-operative Societies Act, 1960,	-- do --
(6)	A registered dealer under the Maharashtra Value Added Tax Act, 2002.	-- do --
(7)	Insurance or Financial Corporation or Company; and any Bank included in the Second Schedule to the Reserve Bank of India Act, 1934, and any Scheduled Bank recognized by the Reserve Bank of India.	-- do --

(8)	Trusts, whether public or private	-- do --
(9)	A Co-operative Housing Society registered under the Maharashtra Co-operative Societies Act, 1960 which has awarded contracts of value aggregating to rupees 10 lakhs or more in the previous year or as the case may be, in the current year.	-- do --

iv) The rates of TDS are prescribed at 2% if the contractor is registered dealer and 4% if the contractor is unregistered dealer.

v) The TDS is not to be made when the payment or aggregate of payment to the contractor in a year is less than Rs.5 lakhs. In other words it will apply when the payments are exceeding Rs. 5 lakhs. In case of Cooperative Housing Society the TDS provision will apply if it has awarded contract more than Rs.10 lakhs in previous year or current year.

vi) The TDS is to be deducted from net amount and no TDS is required to be deducted from sales tax or service tax separately charged by the contractor.

vii) TDS should not exceed the tax payable by such contractor.

viii) TDS should not apply to contracts taking place in course of inter-state trade or in course of import/ exports.

ix) No TDS is required when principal contractor is making payment to sub-contractor.

x) In relation to advance payment, the TDS will apply as and when the advance payment is adjusted towards the actual amount payable to the contractor.

xi) There are provisions for obtaining certificates for no deduction. The application is to be made in Form No. 410.

xii) The credit of TDS should be available to dealer from whose payment the TDS is deducted. The credit will be available in the relevant period in which TDS is deducted or certificate is obtained.

xiii) The employer failing to deduct or after deduction failing to pay to Government, will be considered to be dealer in arrears and other provisions of Act including payment of interest will apply to him accordingly.

xiv) Challan No. 210 is to be used for depositing the tax deducted.

xv) The TDS amount should be paid within 21 days from end of the month in which TDS is deducted, irrespective of the amount of TDS.

xvi) Annual TDS return in Form No. 405 is required to be filed before the Joint Commissioner (Returns) in Mumbai and with Joint Commissioner (VAT Administration) in the rest of the State, within three months from the end of relevant accounting year.

xvii) Unregistered employers who have deducted tax at source, on payments made to the contractors, are required to file Chalan No. 210 alongwith demand draft/ pay order and photocopy of his PAN card before the Deputy Commissioner of Sales Tax (E-810), Business Audit(2), Vikrikar Bhavan, Mazgaon for Mumbai location and concerned Sales Tax Officer, Returns Branch for rest of the Maharashtra locations. For Mumbai location, the employers should draw demand draft/ pay order in favour **of the Bank of Maharashtra A/c MVAT payable at Mumbai.** For rest of the Maharashtra, the employers should draw demand draft/ pay order in favour of **the S.B.I. A/c MVAT payable at respective locations.(Refer Circular No.42T of 2008 dt.26.12.2008).**

xviii) The employer should issue TDS certificate to the contractor. The TDS certificate should be in form 402 and be issued after payment of TDS is made in Government Treasury.

xix) The employer should maintain a separate register of TDS in Form 404.

CONCLUSION

The topics relating to tax legislations are evergreen topics as day-to-day new developments go on. In addition to amendments to the Provisions, there are changes due to judgments and interpretations. Also in the field of tax legislation each case is a unique case and the tax implications depend on facts of the said case. Therefore no standard theory can be laid down for any kind of tax implications. The above note is with an intention to discuss issues under VAT relating to construction industry. I hope participants will find above note useful in their day-to-day practice while dealing with the subject of sales tax implications on Construction Industry. I wish a grand success to the seminar.