



Computation & Assessment of Vat on Builders/Developers- Post L&T (SC)

by CA Deepak Thakkar,

Mumbai

at WIRC of ICAI at Mumbai, dt 20 Dec 2013



L&T Ltd & ors vs State of Karnataka & ors

Civil Appeal # 8672 of 2013 Order dt 26 Sept 2013 (SC)
Larger Bench of 3 Judges (R M Lodha J, J Chelameswar J, M B Lokur J).....

- SC LB reconsidered its Division Bench ruling in **K. Raheja Development Corpn v. State of Karnataka; (2005) 5 SCC 162** as referred by its Division bench ruling in **L&T Ltd & Anr. v. State of Karnataka & Anr. SLP(C) No. 17741 of 2007**
- SC considered 14 appeals from Karnataka & 12 appeals from Maharashtra thus in all 26 appeals decided which include Promoters & Builders Asso. filed SLP # 17738 & 17709 of 2012 **MCHI filed SLP (Civil) #21934 of 2012 dt 4 July 2012?**
- SC ruling after 6 months of hearing, by LB of 3 Judges, for 26 appeals, running in 83 pages & 126 paras, referring 61st Law Commissions Report, 46th Amendment to Constitution, 28 prominent case laws of SC, English & Australian Court

.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
Computation of Value of goods involved in WC:

Observations of SC:

- **Para 68:** "Though the tax is imposed on the transfer of property in goods involved in the execution of a works contract, the measure for levy of such imposition is the **value of the goods involved in the execution of a works contract**. Since, **the taxable event** is the transfer of property in goods involved in the execution of a works contract and the said transfer of property in such goods takes place when the goods are incorporated in the works, **the value of the goods which can constitute the measure for the levy of the tax has to be the value of the goods at the time of incorporation of the goods in works and not the cost of acquisition of the goods by the contractor.**"
- **Para 70:** "The Forty-sixth Amendment leaves no manner of doubt that the States have power to bifurcate the contract and **levy sales tax on the value of the material involved in the execution of the works contract**. The States are now empowered to **levy sales tax on the material used in such contract**. In other words, clause 29-A of Article 366 empowers the States to levy tax on the deemed sale."

17 Dec 2013

3

.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
SC summarises legal position qua WC in sale of a unit in
under construction building at Para 101:

- **Para 101:** SC summarises legal positions for levy of sales tax on goods involved in sale of a unit in under construction building :
- **Para 101(i):** "(i) For sustaining the levy of tax on the goods deemed to have been sold in execution of a works contract, three conditions must be fulfilled:
(one) there must be a works contract,
(two) the goods should have been involved in the execution of a works contract and
(three) the property in those goods must be transferred to a third party either as goods or in some other form."
- **Para 101(ii):** "**For the purposes of Article 366(29-A)(b), in a building contract or any contract to do construction, if the developer has received or is entitled to receive valuable consideration, the above three things are fully met.** It is so because in the performance of a contract for construction of building, the goods (chattels) like cement, concrete, steel, bricks etc. are intended to be incorporated in the structure and even though they lost their identity as goods but this factor does not prevent them from being goods."

17 Dec 2013

4



.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
SC summarises legal position qua WC in sale of a unit in under construction building at Para 101:

- **Para 101(iii): "Where a contract comprises of both a works contract and a transfer of immovable property, such contract does not denude it of its character as works contract.** The term "works contract" in Article 366 (29-A)(b) takes within its fold all genre of works contract and is not restricted to one specie of contract to provide for labour and services alone. **Nothing in Article 366(29-A)(b) limits the term "works contract".**
- **Para 101(iv): "Building contracts are species of the works contract."**
- **Para 101(v): "A contract may involve both a contract of work and labour and a contract for sale. In such composite contract, the distinction between contract for sale of goods and contract for work (or service) is virtually diminished."**
- **Para 101(vi): "The dominant nature test has no application and the traditional decisions which have held that the substance of the contract must be seen have lost their significance where transactions are of the nature contemplated in Article 366(29-A).... The enforceability test is also not determinative."**

17 Dec 2013

5



.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
SC summarises legal position qua WC in sale of a unit in under construction building at Para 101:

- **Para 101(vii): "A transfer of property in goods under clause 29-A(b) of Article 366 is deemed to be a sale of the goods involved in the execution of a works contract by the person making the transfer and the purchase of those goods by the person to whom such transfer is made."**
- **Para 101(viii): "Even in a single and indivisible works contract, by virtue of the legal fiction introduced by Article 366(29-A)(b), there is a deemed sale of goods which are involved in the execution of the works contract. Such a deemed sale has all the incidents of the sale of goods involved in the execution of a works contract where the contract is divisible into one for the sale of goods and the other for supply of labour and services. In other words, the single and indivisible contract, now by Forty-sixth Amendment has been brought on par with a contract containing two separate agreements and **States have now power to levy sales tax on the value of the material in the execution of works contract."****

17 Dec 2013

6

.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
SC summarises legal position qua WC in sale of a unit in
under construction building at Para 101:

- Para 101 (xi): **“Taxing the sale of goods element in a works contract under Article 366(29-A)(b) read with Entry 54 List II is permissible even after incorporation of goods provided tax is directed to the value of goods and does not purport to tax the transfer of immovable property. The value of the goods which can constitute the measure for the levy of the tax has to be the value of the goods at the time of incorporation of the goods in works even though property passes as between the developer and the flat purchaser after incorporation of goods.”**

17 Dec 2013

7

.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
K. Raheja Dev. Corp. vs St of Karnataka (2005) 5 SCC
162 (SC) referred to:

- Para 107: Raheja Development’s SC ruling reproduced:
 - “(i) The definition of the term “works contract” in the Act is an inclusive definition.
 - (ii) It is a wide definition which includes “any agreement” for carrying out building or construction activity for cash, deferred payment or other valuable consideration.
 - (iii) The definition of works contract does not make a distinction based on who carries on the construction activity. **Even an owner of the property may be said to be carrying on a works contract if he enters into an agreement to construct for cash, deferred payment or other valuable consideration.**
 - (iv) **The developers had undertaken to build for the prospective purchaser.**
 - (v) Such construction/development was to be on payment of a price in various installments set out in the agreement.”

17 Dec 2013

8

.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
K. Raheja Dev. Corp. vs St of Karnataka (2005) 5 SCC 162
(SC) referred to:

- Para 107: Raheja Development's SC ruling reproduced:
 - “(vi) The developers were not the owners. They claimed lien on the property. They had right to terminate the agreement and dispose of the unit if a breach was committed by the purchaser. A clause like this does not mean that the agreement ceases to be “works contract”. So long as there is no termination, the construction is for and on behalf of the purchaser and it remains a “works contract”.
 - (vii) If there is a termination and a particular unit is not resold but retained by the developer, there would be no works contract to that extent.**
 - (viii) If the agreement is entered into after the flat or unit is already constructed then there would be no works contract. But, so long as the agreement is entered into before the construction is complete it would be works contract.”**

17 Dec 2013

9

.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
**Taxable Event in building construction: Stage from which vat
liable: Importance of date of contract with flat buyer:**

- Para 115: “It may, however, be clarified that activity of construction undertaken by the developer would be works contract only from the stage the developer enters into a contract with the flat purchaser. The value addition made to the goods transferred after the agreement is entered into with the flat purchaser can only be made chargeable to tax by the State Government.”
- Para 117: “The submission of Mr. K.N. Bhat (Karnataka Govt) that the view in Raheja Development that when a completed building is sold, there is no work contract and, therefore, no liability to tax is not correct statement of law, does not appeal to us. If at the time of construction and until the construction was completed, there was no contract for construction of the building with the flat purchaser, the goods used in the construction cannot be deemed to have been sold by the builder since at that time there is no purchaser. That the building is intended for sale ultimately after construction does not make any difference.”

17 Dec 2013

10

Taxable Event in building construction: Stage from which vat liable: Importance of date of contract with flat buyer....:

Milestone or Stages	Stage of Construction	Goods used	Approx. value %
1st	Upto Plinth Level or Podium (Piling, Basements, Ground flr)	Steel, Stones, Cement, RMC, etc	??
2nd	RCC framework for Floorwise Slabs	Steel, Stones, Cement, RMC, etc	??
3rd	Masonry work	Bricks, sand, cement or Ciporax or Concrete block	??
4th	Plaster: Internal & External	Sand & cement or Gypsum	??
Total value from 1st to 4th stage			Steel 18% & Concrete 18% = Total 36%

17 Dec 2013

11

...Taxable Event in building construction: Stage from which vat liable: Importance of date of contract with flat buyer:

Milestone or Stages	Stage of Construction	Goods used	Approx. value %
5th	Doors & Windows	Timber, Metal, fittings, etc	
6th	Flooring & Tiling	Tiles, Marble, Granite, etc	
7th	Plumbing, Sanitary & Electrical work	Pipes, fittings, sanitary wares, cables, switches, fittings, etc	
8th	Lift / Elevators	Lift	
9th	Painting: Internal & External	Paints, chemicals, etc	
10th	Compound flooring, walls, landscape, etc	Tiles, pavers, bricks, gates, etc	
Certificate of Architect or Civil Engineer or Qty. Surveyor oror Accounts ??			Total value from 5th stage to 10th stage 24% So Total goods = 60%
11 th	Application for OC/CC	Grant of OC / CC after 3 / 6 / 12 months	

17 Dec 2013

12

Example for Vat Computation for Builder/Developer (Rs. in Lacs)...

Contract During	Agreement	Land Value	Constrn. Stage Dedn.	Bal.	Labour (25% to 40%)	Material (60% to 75%)
Project Launch	100	20	Zero = 0	80	20/24/30	60/56/50
Stage 1	111	20	10% = 9	82	21/25/30	61/57/52
Stage 4	102	30	30% = 22	50	12/16/20	38/34/30
Stage 10	113	30	90% = 75	8	2/3/4	6/5/4
OC Applied	114		100%			No T.O.P = No Vat ?
OC Grant	115		100%			No T.O.P = No Vat

17 Dec 2013

13

...Example for Vat Computation for Builder/Developer (Rs. in Lacs)

Contract During	Agreement	Material (60% to 75%)	Gross VAT (4% - 12.5%)	Set-off	Net VAT
Project Launch	100	60/56/50	7/6/5	4/3/2	3/3/3
Stage 1 (10%)	111	61/57/52	7/6/5	4/3/2	3/3/3
Stage 4 (30%)	102	38/34/30	4/3/3	2/1/1	2/2/2
Stage 10 (90%)	113	6/5/4	1/1/1	0/0/0	1/1/1
OC Applied (100%)	114	No T.O.P = No Vat	Zero?	Zero?	Zero?
OC Grant	115	No T.O.P = No Vat	Zero	Zero	Zero

17 Dec 2013

14

.....L&T Ltd & Ors vs St of Karnataka & Ors 26-9-13 SC:
Approval of K. Raheja Dev. Ruling dt 5-5-2005 SC:

- Para 118. "We are clearly of the view that Raheja Development lays down the correct legal position and we approve the same."
- Para 121: ".....Thus, in our view, there is no merit in the challenge to the constitutional validity to the provisions of explanation (b)(ii) to Section 2(24) of MVAT which were amended with effect from 20.06.2006...."
Excerpts from Para 34 of BHC decision in MCHI:
" **Whether there is a works contract in a given case is for assessing authorities to determine....**
..... **the amended definition in the State legislation in the present case provides a clarification or clarificatory instances....**"
- Para 122: "We are in agreement with the above view and reject challenge to amendment to the provisions of explanation (b)(ii) to Section 2(24) of MVAT Act."

17 Dec 2013

15

.....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
Mode of valuation of goods provided under Rule 58(1A)
needs clarity from Maharashtra State Govt:

- Para 123: "Sub-rule (1A) was inserted into Rule 58 by a notification dated 01.06.2009....
..... The challenge was laid to Rule 58(1A) of the MVAT Rules before the Bombay High Court....."
- Para 124: "The value of the goods which can constitute the measure of the levy of the tax has to be the value of the goods at the time of incorporation of goods in the works even though property in goods passes later. Taxing the sale of goods element in a works contract is permissible even after incorporation of goods provided tax is directed to the value of goods at the time of incorporation and does not purport to tax the transfer of immovable property. The mode of valuation of goods provided in Rule 58(1A) has to be read in the manner that meets this criteria and we read down Rule 58(1-A) accordingly. The Maharashtra Government has to bring clarity in Rule 58 (1-A) as indicated above. Subject to this, validity of Rule 58(1-A) of MVAT Rules is sustained."

[So Land cost or land value as per SDRR, whichever higher ?? Evidence??]

17 Dec 2013

16

Issues for Land Value Deduction u/r 58(1A)

- Cost of land shall be determined as per Guidelines to Stamp Duty Ready Reckoner (SDRR)
- Cost if zero, still deduction available?
- Cost, if more than value as per SDRR, allowable?
- SDRR Land rate given per square mtr, whether to apply directly to area of each unit or area of plot & then to apply to each unit proportionately?
- SDRR Land rate given for FSI 1:1 which shall be enhanced by 40% if TDR loaded on said land; or FSI 3:1?
- TDR cost can be added to land cost?
- Corpus fund, rent, etc given to existing occupants in redevelopment project can be added to land cost?
- Constructed area given free to Land Owner...Value?
- SDRR Land rate is issued as on 1st Jan every year which is applicable to agreements registered in that calendar year

17 Dec 2013

17

Rate of Construction cost, per built-up square mtr., as per Stamp Duty RR Mumbai, for RCC frame (Pukka) Structure; Guidelines issued by Chief Controlling Revenue Authority & Inspector General of Registration, Maharashtra: Can we adopt said value for Vat?

C.Y.	Mumbai Suburb Rs.	Mumbai City Rs.	Material Value @ 70% u/r 58	Gross Vat (4% to 12.5%)	Gross Vat per Sqr. Ft. (@10.764)	Net Vat after setoff
2006	7,500	8,500	5,950	536	50	
2007	8,000	9,000	6,300	567	53	
2008	10,000	12,000	8,400	756	70	
2009	10,000	12,000	8,400	756	70	
2010	11,000	13,000	9,100	819	76	
2011	15,000	16,000	11,200	1,008	94	
2012	16,000	17,500	12,250	1,103	103	

17 Dec 2013

18

....L&T Ltd & Ors vs St of Karnataka & Ors dt 26-9-13 SC:
Mah. AG assures that implementation of Rule 58(1A) shall not result in double taxation; Circulars are only clarificatory in nature, so not binding to tax payer:

- Para 125: “Once we have held that Raheja Development¹ lays down the correct law, **in our opinion**, nothing turns on the circular dated 07.02.2007 and the notification dated 09.07.2010. **The circular is a trade circular which is clarificatory in nature only.** The notification enables the registered dealer to opt for a composition scheme. The High Court has dealt with the circular and notification. **We do not find any error** in the view of the High Court in this regard. **Moreover, the Advocate General for Maharashtra clearly stated before us that implementation of Rule 58(1-A) shall not result in double taxation and in any case all claims of alleged double taxation will be determined in the process of assessment of each individual case.**”

Double taxation qua: sub-contract; stamp duty & vat; Land value deduction; etc??

- Para 126: “**After having given answer to the reference, we send the matters back to the Regular Bench for final disposal.**”

17 Dec 2013

19

Way Forward Post L&T SC 26-9-13

- **BAI SLP in SC dt 7 Mar 2013 against BHC order dt 30 Oct 2012, hearing on 13 Dec. 2013 (Challenged Trade Cir# 14T dt 6 Aug 2012 of Adm. Relief & 18T dt 26 Sep 2012 rejecting Cost plus method)**
- Await for ruling from regular bench of SC in respective cases (MCHI, BAI, Promoters & Builders Asso., etc)
- Maharashtra Govt has to bring in clarity in Rule 58(1A) to grant proper deduction for value of land (Cost, FSI, TDR, SDRR, etc) & labour (various clauses) to arrive at value of goods which can be taxed as directed by SC in Para 124 of ruling
- Maharashtra Govt shall implement Rule 58(1A) such that it shall not result in double taxation in any case as committed by AG before SC in Para 125
- Computation Rule shall be modified such that goods used **till the stage of execution of the agreement with flat purchaser** is not taxed as held by SC in Para 115 & 117
- Till above verdict of SC is honored, assessment cannot be made & recovery be stayed
- BHC Ruling dt 30 Oct 2012 in Ashok R Gokani & Marathi Bandhkam Asso. held that “whether a contract constitutes a WC or involves an element of WC is a matter which shall be decided on facts of individual case in accordance with provisions of MVAT Act”

17 Dec 2013

20

Way Forward Post L&T SC 26-9-13

- ADM relief orders shall be passed soon (2 days mentioned in circular) as confirmed by Commissioner in Trade Circular # 14T dt 6 Aug 2012 & 17T dt 25 Sep 2012
- Coercive recovery of tax, interest or penalty shall remain stayed in cases where dealer followed Trade Circular # 17T dt 25 Sep 2012 & obtained registration on or before 15 Oct 2012 and paid taxes & filed Returns upto 31 Oct 2012 as per directions of SC. The said payment shall be subject to final decision of SC.
- **Interest & penalty** shall not be levied in such a case where basic levy & computation mechanism is before SC abinitio; Govt shall be fair to taxpayer
- **New projects of RD Developers**, shall apply composition scheme of 1% of agreement value or stamp duty value, whichever higher, or vat provisions, depending upon facts of each case.

17 Dec 2013

21

Time barring of assessment u/s 23 of MVAT Act

Section	Circumstance	Fin. Year	Time barring date	Remark
23(3A)	RD filed Returns in-time or late then pass assessment order within 7 yrs from end of the yr	2005-06	30 Jun 2013	Proviso to sec. 23(3A)
23(3A)	----do----	2006-07	31 Mar 2014	
23(3A)	----do----	2007-08	31 Mar 2015	
23(2)	RD filed Returns in-time then pass assessment order within 4 yrs from end of the year;	2008-09	30 Jun 2013	3 rd Proviso to sec. 23(2)
23(2)	----do----	2009-10	31 Mar 2014	
23(2)	----do----	2010-11	31 Mar 2015	and so on....

17 Dec 2013

22

Time barring of assessment u/s 23 of MVAT Act

Section	Circumstance	Fin. Year	Time barring date	Remark
23(3)	RD filed Returns then pass assessment order within 5 yrs from end of the year;	2008-09	31 Mar 2014	Developer late getting Adm relief as per Trade Circular # 14T dt 6 Aug 2012 & 17T dt 25 Sep 2012
23(2)	----do----	2009-10	31 Mar 2015	
23(2)	----do----	2010-11	31 Mar 2016	and so on....
23(4)	URD / URD period, then pass assessment order within 8 yrs from end of the year	2005-06	31 Mar 2014	and so on....

17 Dec 2013

23

Time barring of assessment u/s 23 of MVAT Act

Section	Circumstance	Fin. Year	Time barring date	Remark
23(5)	Assessment of any Transaction where tax is evaded or excess setoff is claimed, initiate assessment in any search or other proceedings	???	???	Again no tax on said transaction under any provision (Proviso to sec. 23(5)(d)); and so on...
23(6)	Assessment of any undisclosed turnover or tax paid at lesser rate or setoff/deduction wrongly claimed, then pass order within 6 yrs of end of the year	2007-08	31 Mar 2014	and so on...

17 Dec 2013

24



Time barring of assessment u/s 23 of MVAT Act

Section	Circumstance	Fin. Year	Time barring date	Remark
23(7)	Fresh assessment to give effect to any finding or direction contained in any order made by Tribunal or HC or SC, pass order within 36 mths from the dt of receipt of said order by Commr.	2006-07 & 2008-09	31 Mar 2014	
23(7)	----do----	2007-08 & 2009-10	31 Mar 2015	and so on...

17 Dec 2013

25



Time barring of assessment u/s 23 of MVAT Act

Section	Circumstance
23(1)	RD fails to file return for any period within time, results in ex-parte assessment, within 3 yrs from end of the yr, without hearing dealer; If dealer submits the return then said assessment order shall stand cancelled; (Automatic cancellation wef 1 May 2013)
23(8)	Assessment order passed without considering decision of Tribunal given against the State or Commr, if an appeal is filed against said order which is pending; No order of recovery of tax, interest, penalty or forfeiture be passed in such case till final decision & hearing
23(9)	Dealer may apply in Form 305 to Commr for issuance of direction to assessing authority for guidance, which is binding on authority
23(11) & (12)	Ex-parte assessment made u/s 23(2) or (3) or (4) for non-attendance & when dealer applies in Form 316, within 30 days of service of said order, then make fresh assessment within 18 mths from the date of service of cancellation order; Dealer can apply only once in respect of any period of assessment

17 Dec 2013

26

“Bridge & Wall are made with same **material**,
but Bridge joins people & Wall divides people”

17 Dec 2013

27

