DEPARTMENT OF COMMERCIAL TAXES, KERALA
PROCEEDINGS OF THE AUTHORITY FOR CLARIFICATION
U/s.94 OF THE KERALA VALUE ADDED TAX ACT, 2003.

Members present are:

1. ***K.J. Valsala Kumari, Joint Commissioner (General), O/o. CCT, Tvpm.***
2. ***T.V. Kamala Bai, Joint Commissioner (Law), O/o. CCT, Tvpm.***
3. ***S.K. Suchala Kumar, Joint Commissioner (Audit & Inspection), O/o. CCT, Tvpm.***

Sub :- KVAT Act, 2003 – Clarification U/s 94 – Works Contract, liability to take out registration under the Act and deduction of tax at source – Orders issued.

Read :- Application from M/s. Fi Desighn & Development Pvt. Ltd., Bangalore dtd. 21/6/2012.

ORDER No.C3/20005/12/CT DATED 14/11/2012.

1. M/s. Fi Desighn & Development Pvt. Ltd., Bangalore has preferred an application U/s 94 of the Kerala Value Added Tax Act, 2003 seeking clarification on the liability to take out registration and deduction of tax at source under the Act with regard to works contract.

2. The applicant is a company incorporated under the provisions of the Companies Act, 1956 and having its registered office at Bangalore, engaged in construction and designing for its clients. The services provided by the applicant includes:

Interior Designing
Solutions in Spatial Design

3. The applicant has received a work order from Indian Institute of Management, Kozhikode (IIM-K) for setting up of the Business History Museum at IIM-K Campus. Pursuant to the work order, IIM-K and the applicant entered into an agreement for undertaking the work vide agreement dated 2/9/2011. IIM-K has given the constructed shell building to the applicant for interior designing and undertaking the interior work which is a composite activity of labour and material. The materials primarily comprise of wooden panels, electronic items, miscellaneous construction related materials etc.

4. The materials for undertaking the contract were procured by the applicant from Bangalore (Karnataka) either directly or through sub contractors and brought to Kozhikode (Kerala) where the work was undertaken.

5. The applicant has been treating the same as interstate works contract and charging Central Sales Tax (CST) on the same. IIM-K has proposed to deduct tax at source on the sums paid to the applicant.

6. The applicant would contend that, in the present case, since all the goods were procured from Bangalore (Karnataka) and brought to Kozhikode (Kerala) for execution of the work at Kozhikode (Kerala), there is an inter-state movement of goods, thereby resulting in the transaction being an inter-state works contract. The gist of the contentions raised by the applicant can be summarized as follows:

After the 46th Constitutional Amendment and the consequent amendments to the Sales Tax enactments including Central Sales Tax Act, 1956, a transfer of property in goods involved in the execution of a works contract is deemed to be a sale transaction. Once it is deemed to be sale transaction under CST, all the principles formulated under Section 3 of the CST for determining whether a sale is an inter-State sale or not, are equally applicable to a sale by way of works contract as held by the Hon'ble Supreme Court in the case of Builders Association. Thus there can be interstate sale by way of works contract if there is an inter-state movement of goods from one state to another pursuant to an agreement.

The provisions of the various State legislations for VAT are applicable for works contract only when the sale (by way of works contract) is a local sale. When a sale (by way of works contract) amounts to an inter - state sale, then it will be outside the powers of the State authorities to levy local Sales Tax on such sale.

The Hon'ble Supreme Court in the case of Steel Authority of India Ltd. Vs. State of Orissa and Naptha Jhakri Jt. Venture Vs. State of UP, held that a State cannot enact a provision requiring an awarder to deduct TDS on the value of works contract representing inter - state sale by way of works contract. Further, in the case of Gannon Dunkerley Vs. State of Rajasthan, it was observed by the Hon'ble Supreme Court that it is necessary to exclude from the value of a works contract the value of the goods which are not taxable by the State in view of sections 3, 4 and 5 of the CST Act, 1956.

Further, the Hon'ble Chhattisgarh High Court in the case of VTP Construction Vs. State of Chattisgarh has also held that Section 35 of the Chhattisgarh Commercial Tax Act, 1994 is ultra vires the constitution in the light of the above decisions of the Hon'ble Supreme Court to the extent it authorizes deduction of TDS with respect to inter - state works contract. The Hon'ble Supreme Court in the case of Rapti Commission Agency VS. State of UP followed SAIL Case and Nathpa Jhakri case and held that the States do not have the power to provide for deduction of TDS on inter-state works contract. The Court further held that if a person is not liable for payment of tax at all, at any time, the collection of a tax from him, with a possible contingency of refund at a later stage, will not make the original levy valid, because if sales or purchases are exempt from taxation altogether, they can never be taken into account, at any stage, for the purpose of calculating or arriving at the taxable turnover and for levying tax. It is no solace to say that such a person can get refund after completion of assessment. The Court felt that if the principles indicated in these cases are followed, large number of unnecessary litigations can be avoided.

Similarly, the Gujarat High Court in the case of Larsen & Toubro Ltd. Vs. Commissioner of Sales Tax, Gujarat and others held that if the State Legislature had no power to impose tax on inter - state sales or sales in the course of import or outside sales through the amount of bill for works contracts, even machinery provisions cannot be made to collect such tax in advance by assuming all the transactions of sales or supplies to be inter - state sales and taxable in the State. The provisions of Section 57 - B of the erstwhile Gujarat Sales Tax Act, 1969 were held to be invalid.

It follows from the above that where a works contract is subjected to CST or in other words where a works contract is executed in the course of inter-state trade or commerce, no TDS shall be made from the contract price.

7. The applicant has placed his reliance on the Order No.C3/24336/11/CT dtd. 28/3/2012 to support his contentions.

8. The applicant would further contend that in the present case since the goods commenced movement from Karnataka, the applicant would be liable to discharge the Central Sales Tax liability in the originating state, i.e. Karnataka. In such a situation Kerala would not have the power to subject the transaction to TDS. In any case, Section 10 of the Kerala Value Added Tax Act which provides for TDS is not attracted in view of the fact that the applicant is not a works contractor liable to pay tax under Section 6 of the Kerala Value Added Tax Act, 2003 in as much as the applicant is liable to tax only under the Central Sales Tax Act in Karnataka.

9. The applicant has requested to clarify the following points:

a. Whether TDS is to be made by IIMK on the payments made to the applicant with respect to the current work undertaken where goods involved has moved from Karnataka to Kerala.
b. Whether the applicant is required to take registration under the Kerala Value Added Tax Act, 2003 and discharge Kerala VAT when the goods involved in the current work has moved from Karnataka to Kerala.

10. The authorised representative of the applicant was heard in the matter and the contentions raised were examined.

11. In case, the movement of goods from outside the State happens for executing works contract in this State in pursuance of an agreement, their occurs inter-state sale within the meaning of Section 3 of the Central Sales Tax Act, 1956; and in the case of execution of work, the situs of such sale is at the State where the goods were situated at the time of appropriation of such goods as per agreement perse (Section 4(2) of the Central Sales Tax Act). Tax shall be collected by that Government in the State from which the movement of the goods commenced as per Section 9(1) of the Central Sales Tax Act, 1956).

12. The proviso to Rule 42(2) of the Kerala Value Added Tax Rules, 2005 states that no amount shall be deducted where the payment relates to that portion of a contract which relates to transfer of goods involved in the execution of works contract, other than those executed in the State.

13. The question regarding inter-state sale is to be answered on the basis of Section 3 of the Central Sales Tax Act, 1956 [Bharat Heavy Electricals Ltd. Vs. Union of India 102 STC 382 (SC)]. The law requires that, it should be levied and collected in the State from which the movement of goods commences. The movement in pursuance of an agreement is the main criteria for fixing the situs of taxation. Further in Indian Oil Corporation [47 STC 5], it was held that a sale is an inter-state sale under Section 3 of the Central Sales Tax Act, 1956 if there is a contract of sale preceding the movement from one State to another and the movement must be the result of this covenant. In Larsen & Toubro Ltd. Vs. Commissioner of Commercial Taxes, AP [(2003) 132 STC 272 (AP)], the Andhra Pradesh High Court held that commodities were brought from Mumbai in pursuance of an agreement and hence it would come within the ambit of inter-state sale under Section 3 of the Central Sales Tax Act, 1956. Hence it can be summarized that the provisions of the agreement must precede the

movement of materials from one State to another to come within the ambit of Section 3 of the Central Sales Tax Act, 1956.

14. The importance of the provisions of the agreement in works contracts have been highlighted in a number of judgments. The nature of the contract is to be verified on the totality of its terms and conditions [Cradle Runways India Vs. Commissioner of Commercial Taxes, Karnataka (2006) 144 STC 465 (Kar)]. The questions regarding the transaction may be determined on the terms of the contract and not from the invoice issued by the person entitled to receive amount under the contract [Arun Electricals Vs. Commissioner of Sales Tax 17 STC 576 (SC)]. The nature of the contract is to be determined by looking into all provisions of the agreement [Construction Co. Vs. State of Kerala 36 STC 320 (Ker)]. Works contract conditions must be established on the basis of agreement between parties [N.V. Shenoy & Co. Vs. Sales Tax Officer 1994 STC 469 (Ker)].

15. Verification of the copy of the agreement between the applicant and Indian Institute of Management, Kozhikode would show that aspects like time schedule for the completion of work, terms of payment etc. have been stated therein. But the agreement is silent as to from where the contractor must procure materials. The contractor is free to procure materials from Kerala or from outside. Hence procuring materials from Karnataka is only a decision of the contractor and it is not in pursuance of an agreement between the parties. In State of Kerala Vs. Unitech Machines Ltd. [(2011) 19 KTR 354 (Ker)]; a works contract case, wherein the contractor procured materials from outside Kerala, the Court held that it cannot be considered within the scope of inter-state works contract.

16. Based on the different Court decisions already discussed and in the light of Section 3 of the Central Sales Tax Act, 1956, if the movement started from another State to this State not in pursuance of an agreement the tax liability at the tax situs cannot be excluded.

17. A condition must be there in the agreement between the parties stipulating the purchase of materials from Karnataka and the movement of the goods from Karnataka should have originated in pursuance of that agreement in order to qualify as inter-state works contract. There is no such condition in the agreement produced by the applicant. The applicant is free to procure from any state or from Kerala. But the applicant, on their own has brought materials from Karnataka. From the documents produced by the applicant it cannot be stated that movement of goods commenced on the basis of the agreement concluded. Verification of the documents produced by the applicant would reveal that they have effected local sale of goods to Indian Institute of Management, Kozhikode, at Bangalore. As stated above there is no specific clause in the agreement regarding supply of goods and nothing has been produced to prove that movement of goods from one State to another happened on the basis of a concluded agreement. Mere issuance of Form No.16 by Indian Institute of Management, Kozhikode would not change the position, and in fact, has created a situation wherein it can be treated as a local sale by Indian Institute of Management, Kozhikode to the petitioner since as per the documents produced, Indian Institute of Management, Kozhikode has procured the material by paying VAT at Karnataka and supplied materials to contractor since its value was also included in the contract.

18. In view of the facts stated supra and also on the basis of the details as revealed from the agreement produced and the bills produced, it can be concluded that the impugned transaction does not amount to an inter-state works contract and it will attract tax under Kerala Value Added Tax Act, 2003 and hence, Indian Institute of Management, Kozhikode is

liable to make tax deduction at source (TDS) under Section 10 of the Act and also, the applicant is liable to take out registration under the Kerala Value Added Tax Act, 2003.

The issues raised above are clarified accordingly.

K.J. Valsala Kumari	**T.V. Kamala Bai**	**S.K. Suchala Kumar**
Joint Commissioner (General)	**Joint Commissioner (Law)**	**Joint Commissioner (A&I)**
O/o CCT	**O/o CCT**	**O/o CCT**

To,

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