

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

1. K.J. Valsala Kumari,
Joint Commissioner (General),
Office of the Commissioner of Commercial Taxes, Thiruvananthapuram.

2. T.V. Kamala Bai,
Joint Commissioner (Law),
Office of the Commissioner of Commercial Taxes, Thiruvananthapuram.

3. S.K. Suchala Kumar,
Joint Commissioner (Audit & Inspection),
Office of the Commissioner of Commercial Taxes, Thiruvananthapuram.

Sub :- KVAT Act, 2003 - Clarification U/s 94 - Tax liability on free supply of diagnostic equipment / instruments under lease agreement by dealers outside the State to hospitals / laboratories in Kerala - Orders issued.

Read :- Application from M/s. All Kerala Scientific & Surgical Dealers Association, Kochi dtd. Nil.

ORDER No.C3/42668/11/CT DATED 29/11/2012.

1. M/s. All Kerala Scientific & Surgical Dealers Association, Kochi has preferred an application U/s 94 of the Kerala Value Added Tax Act, 2003 seeking clarification on the tax liability on free supply of diagnostic equipment / instruments under lease agreement by dealers outside the State to hospitals / laboratories in Kerala.

2. The applicant is a registered association of dealers / distributors in diagnostic materials, reagents and consumables used in equipments / instruments used in diagnostics. The applicant contends that in this line of business, free supply and installation of diagnostic and medical equipments / instruments by the importers outside the State at the premises of hospitals / institutions / pathological laboratories at zero rated invoice is a usual phenomenon. In consideration of such free supply these institutions have to purchase and consume certain minimum value of reagents / chemicals / consumables required for the said equipment from the dealers of the supplier of equipments. The transfer of the equipments is under valid agreement on specific terms and conditions generally described as “**Operating Type Lease (OTL)**”. No price is charged for the leasing of the equipment. But the supplier-company’s reagents / chemicals distributed through the dealers in Kerala should be purchased over a period of time as prescribed subject to a minimum aggregate amount. The

equipment shall at all times remain the property of the supplier unless otherwise decided. Since the equipments are supplied free of cost, the reagents sold to the lessee of the OTL fetch very high value on which State exchequer gets tax. The consideration for the free installation of the equipment is the compulsory sale of reagents and diagnostics of the lessor to the lessee. Since the supply of equipments do not involve any passing of consideration as envisaged in Sec.2(xliii), it will not attract any tax liability as provided in Section 6.

3. The applicant contends that there have been instances of interception of the diagnostic equipments supplied by the manufacturers / importers outside the State for free installation to hospital / pathological laboratories in Kerala on the strength of consignment note, Certificate of Ownership in Form 16 and OTL agreement U/s 47(2) of the Kerala Value Added Tax Act, 2003 by the Commercial Tax Department authorities on suspected attempt at evasion of tax. Such apprehensions and assumptions voiced by the inspecting officers are absolutely untenable. Goods being transported under cover of certificate of ownership and other convincing documents in accordance with the provisions of Section 46(3) of the Kerala Value Added Tax Act, 2003, the presumption of attempt at evasion of tax cannot stand the test of legal principles. The petitioner points out that no consideration passes between the supplier and receiver of the equipment as apparent from the "OTL" agreement and that the goods are in movement in the course of inter-state trade and commerce U/s 3(a) of the Central Sales Tax Act will rule out any presumption of attempt at evasion of tax. Umpteen decisions of various Courts affirm the proposition that a sale cannot be constituted without the element of consideration from the buyer to the seller for the transfer of property in goods. In order to constitute "sale" under the Kerala Value Added Tax Act, 2003, there has to be necessarily transfer of property for valuable consideration. This crucial element being totally absent in the dispatch of the machine, the provisions of the Kerala Value Added Tax Act, 2003 will not be attracted. The applicant has relied on the dictum of the apex court in State of Madras Vs. Gannon Dunkerley reported in (1958) 9 STC 353 and the Kerala High Court decision in M. Jaihind Vs. State of Kerala reported in (1998) 111 STC 0374 to support his case.

4. Further, the requirement in Section 46(3) of the Kerala Value Added Tax Act is fully satisfied in these cases. Also since the goods are in interstate movement U/s 3(a) of the Central Sales Tax Act, 1956 under cover of the documents prescribed under the consignor's State laws, the detention of the goods and realization of security are against the decision of the jurisdictional High Court in Sunitha Diesel Sales & Services Vs. State of Kerala (1996) 4 KTR 348, Baheeg Agencies Vs. STI reported in (1998) 6 KTR 150.

5. It has also been contended that free supply and installation of the diagnostic equipments and instruments will not attract any tax liability in view of the facts and circumstances of the case and the rulings of the Courts. The action of the authorities in detaining the equipments supplied free of cost under the lease agreement scheme and demanding security on suspected attempt at evasion of tax U/s 47(2) of the Kerala Value Added Tax Act, 2003 has been badly affecting the traders attached to the applicant association.

6. The applicant contends that another instance of illegal detention of goods purchased interstate is on the allegation of non-accompanying transporter copy or duplicate copy of the invoice along with the consignment. It has been informed that despite such a stipulation being there in Rule 58(11) of the KVAT Rules, the same shall not govern the interstate purchase and transportation of goods. The legal position is well settled by many decisions of the Courts. Further since the goods are in interstate movement U/s 3(a) of the Central Sales Tax Act under cover of the documents prescribed under the consignor's State laws, the action of the authorities is against the decision of the jurisdictional High Court. In the e-filing scenario sale invoices are prepared as per the provisions of the appropriate State laws eg. "Sugam" invoice has to be generated by logging in the System in Karnataka. There is no relevance in the duplicate or other copies of invoices generated in computer. Copies of the invoices whether duplicate or original makes no difference. In any view of the matter, it is irrational and also untenable to suspect attempt at evasion of tax on the allegation of non accompanying the duplicate copy of bill in the case of goods coming from outside the State U/s 3(a) of the Central Sales Tax Act.

7. The applicant would further submit that they have also been experiencing problems in accounting the purchase of medical / diagnostic equipments and instruments from local VAT dealers paying tax as per invoices in their name, which are installed free of cost to the hospitals / diagnostic labs as per the terms of agreement. The dealers do not want to take any input tax credit on the purchase of the equipments. But the authorities do not allow such transactions.

8. The applicant has requested to clarify the following:

i. That free supply and installation of diagnostic equipment / instrument under the lease agreement by the dealers outside the State to hospitals / pathological laboratories in Kerala under zero rated invoice / documents will not attract tax liability under the Kerala Value Added Tax Act, 2003 and hence transportation of the above goods can be made under cover of the consignment document, lease agreement and certificate in Form 16 issued by the consignee.

ii. That transportation of diagnostic equipments purchased by dealers in Kerala on the strength of invoices charging higher rate of Central Sales Tax issued by the dealers outside the State for the purpose of free installation to hospitals / labs under “OTL” agreements is in accordance with the provisions of law and the detention of such consignments is illegal.

iii. That the consignments from outside the State need not be accompanied with the documents as stipulated in Rule 58(11) of the Kerala Value Added Tax Rules and the interception and demand of security deposit U/s 47(2) for not producing transporter copy / duplicate copy of the invoice is illegal.

iv. That local purchase of medical equipments from VAT dealers and free supply of the same to hospitals / diagnostic labs without availing input tax credit are permissible under the provisions of the Kerala Value Added Tax Act, 2003.

9. The authorized representative of the applicant was heard in the matter and the contentions raised were examined.

10. The applicant has presented a business model wherein certain medical establishments in Kerala are entering into ‘operating type lease agreements’ with non-resident dealers in getting lab / diagnostic equipments, fixing up at the places of these medical establishments and other collateral agreement with these non-resident dealers that the insolvents, chemicals and reagents would be sourced only from the non-resident dealers.

11. The applicant has submitted copies of agreement entered by medical establishments in Kerala and the non-resident parties who supply the diagnostic equipments. Verification of the agreements would show that:

i. In the agreement between M/s. Roche Diagnostics India (Pvt.) Ltd, Mumbai and M/s. KIMS Healthcare Management Limited, Trivandrum and the nonresident supplier, there is a clause which reads *”AND WHEREAS since the User has requested Roche to install the said Equipments, at the said Premises without charging any cost, in consideration of which they shall purchase and consume a certain minimum value of Reagents / Chemicals / Consumables required for the said Equipments”*

ii. In the agreement between M/s. Roche Diagnostics India (Pvt.) Ltd, Mumbai and M/s. ACR Labs (KHRWS), Kottayam, Para 4 reads *“In consideration of Roche installing the said Equipments at the said Premises, the User hereby agrees and undertakes to purchase Reagents / Consumables of the value of minimum Rs.175,000 per month for use in the said Equipments and the ROCHE has agreed to import and supply such Reagents / Chemicals / Consumables for the period of this Agreement.....”*

12. The arrangement by which the diagnostic equipments are set up at the premises of the medical establishments would come within the description of right to use of goods. The non-resident owner in whose name the ownership of the diagnostic equipments lies, permits its use by the medical establishments in Kerala.

13. Section 2(xliii) of the Kerala Value Added Tax Act, 2003 reads “Sale” with all its grammatical variations and cognate expressions means any transfer whether in pursuance of a contract or not of the property in goods by one person to another in the course of trade or business for cash or for deferred payment or for other valuable consideration, but does not include a mortgage, hypothecation, charge or pledge;

Explanation V: - A transfer of right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration shall be deemed to be a sale”

14. The applicant contends that there is nil consideration in this arrangement of setting up diagnostic machinery at the premises of the medical establishments. But the binding agreement of mandatory purchase of chemicals, insolvents and reagents from the non-resident dealer can be taken up as consideration in the sense law prescribes. The volume of purchase of these insolvents/reagents can be quantified in terms of money value. The agreements produced by the applicant would show the minimum money value on which the medical establishments has to effect the purchase.

15. In the impugned case, there is exclusive possession and enjoyment of the diagnostic equipments given to the hospitals located in Kerala and the charges for such right to use is clubbed with the price charged on reagents. Since these are locally executed agreements, liability to tax under right to use will be attracted. But the amount under that account is not discernable from the details furnished.

16. It is mandatory for every dealer residing outside the State, but carrying on business in the State to take out registration under the Kerala Value Added Tax Act, 2003. Since the transaction acquires the character of business, the non-resident dealer who set up the diagnostic equipments at the premises of medical establishments in Kerala has to take out registration under the Kerala Value Added Tax Act, 2003. Further the documents prescribed under the local Act also have to follow when the goods are consigned into the State.

The issues raised above are clarified accordingly.

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To,

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