Volume-47 June -2018 Pages 1-21

SBS Wiki

monthly e-Journal

By

SBS and Company LLP
Chartered Accountants

For Private circulation only

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INCOME TAX

SPECIFIED AGREEMENT & NON-RESIDENT

Contributed by CA Ramprasad T

Finance Act 2017 has introduced sub-section 5A to Sec 45 which provides for chargeability of capital gains on transfer of capital asset being land or building or both under a specified agreement in the hands of assessee being individual or HUF(here in after referred as eligible transferor).

This section overrides the provisions of section 45(1) to the extent of year of chargeability as it is postponed to the year in which Certificate of Completion (COC) for whole or part of the project is issued rather than the year in which capital asset was transferred.

Further, provisions of Sec 45(5A) modified the provisions of Sec 48 to the extent of considering the Stamp Duty Value on the date of issue of COC for the share of eligible transferor in the project increased by monetary consideration received shall be deemed to be the full value consideration accruing or received as a result of transfer, that is to say, the consideration in the hands of eligible transferor would be equal to sum of stamp duty value on date of COC + monetary consideration received by the eligible transferor

Consideration = Stamp Duty Value as on COC + Monetary Consideration

The provisions of Sec 45(5A) shall apply provided eligible transferor has not transferred his share in the project before the issue of COC. That is to say, the transferor should not transfer any of his share before the builder/developer obtains the COC for the project.

With the above background of Sec 45(5A), let us now proceed to analyse the impact from the angle of tax deduction at source to be made by builder/developer when payments were made to the eligible transferor.

If the eligible transferor is Resident:

Section 194-IC inserted by Finance Act 2017 provides that any person responsible for paying to any resident any **monetary consideration** under specified agreement referred to in Sec 45(5A) shall deduct tax@10% on such sum. It should be deducted at the time of credit of such sum to the account of payee or payment, whichever is earlier. However, there would be a mismatch between the tax offered and tax credits. Since the income of the eligible transferor is offered to tax in the year of obtaining COC, the eligible transferor would not show any income when monetary consideration is received from the builder/developer. However, in light of Section 194-IC, the tax has to be deducted at the earliest of payment or credit, the builder/developer would deduct tax on payment of monetary consideration to the eligible transferor. Hence, in all cases, there would be a mismatch of tax credits. The eligible transferor would have tax credit in a year which would be different from the year in which his income is offered for tax.

In such a situation, the eligible transferor can carry forward the tax credit in accordance with Section 199 of Income Tax Act read with Rule 37BA(3)(i) of Income Tax Rules, 1962.

If the eligible transferor is Non- Resident:

There is no restriction on applicability of Section45(5A) to the Non-Resident Indian who has entered specified agreement as owner of the capital asset. The section does not distinguish between the resident and non-resident eligible transferor and accordingly the non-resident Indian can avail the benefit of Section 45(5A) subject to the conditions enshrined therein.

However, if the eligible transferor is a non-resident Indian, the tax deduction at source has to be done under section 195 instead of Section 194-IC. The tax has to be deducted by the builder/developer on monetary consideration paid to the eligible transferor who is a non-resident Indian.

As per the provisions of Sec 195(1) any person responsible paying to non-resident any interest or other sum chargeable to tax (other than salary) shall deduct tax at the rates in force. Tax should be deducted at the earliest of credit or payment to the non-resident.

The issue for consideration is, whether TDS should be made under Section 195 at the time of payment of monetary consideration to the non-resident under the specified agreement though capital gain is not chargeable to tax in the year of payment? In other words, as stated supra, there is always a timing difference between the tax deduction at source and income offered to tax by the eligible transferor. In such a scenario, whether the builder/developer is constrained to deduct tax on monetary consideration payable to the eligible transferor despite, the latter's income is not subjected to tax in such year when he receives payment from builder/developer? Let us proceed to analyse the provisions to arrive at a conclusion.

Section 195(1) mandates deduction of tax only the s***um chargeable under the provisions of the Income tax Act.*** In other words, if the income is not chargeable to tax under the provisions of the Income Tax Act, there would be no applicability of Section 195. This is also blessed by the apex court in the case of GE India Technology Cen. (P.) Ltd vs Commissioner of Income Tax, [2010] 193 Taxman 234 (SC). Para 9 of the said judgment is reproduced hereunder for ready reference:

This reasoning flows from the words "sum chargeable under the provisions of the Act" in section 195(1). The fact that the revenue has not obtained any information per se cannot be a ground to construe section 195 widely so as to require deduction of TAS even in a case where an amount paid is not chargeable to tax in India at all. We cannot read section 195, as suggested by the Department, namely, ***that the moment there is remittance the obligation to deduct TAS arises. If we were to accept such a contention it would mean that on mere payment income would be said to arise or accrue in India. Therefore, as stated earlier, if the contention of the Department was accepted it would mean obliteration of the expression "sum chargeable under the provisions of the Act" from section 195(1).*** *While interpreting a section one has to give weightage to every word used in that section.*

The year of taxability as per Sec 45(5A) is the year in which COC for the whole or part of project is issued. The monetary consideration received as a part of consideration under specified agreement will be chargeable to tax in the later year in which COC is issued.

So, one would argue that when monetary payment was made, no TDS is required under Section 195 as income is not chargeable to tax in India at that time because of provisions of Sec 45(5A) and reading with the apex court judgment.

Hence, the payer that is builder/developer can delay the deduction of tax under Section 195 when payment of monetary consideration is made to eligible transferor. However, this would present another problem.

Let us assume, the builder/developer does not deduct tax in the year of payment of monetary consideration and plans to deduct in the year when the non-resident Indian transferor income is offered to tax that is in the year when COC Is obtained. In such a case, the builder/developer has to deduct tax on the Capital Gain (if the cost of acquisition is known to him, otherwise on the net consideration).

However, a situation may arise where in the year of issue of COC builder/developer is not required to pay any monetary consideration (as explained in the below example) as such,it will be difficult to comply with TDS provisions.

Ex: Mr. A, NRI has entered in to Specified agreement with a developer in India. As per the agreement the NRI will receive Rs. 1Crore and 10flats in the developed property.

Consideration is as follows:-

Year I	Year II	Year III/ Year of issue of COC
Monetary Consideration of Rs. 30,00,000/-	Monetary Consideration of Rs.70,00,000/-	10 Flats. Stamp Duty Value is Rs. 40 Lakhs per flat. Total non-monetary consideration is Rs.4Cr

Assume the cost of acquisition of property transferred is Rs. 1.5 Cr the resultant capital gain is Rs. 3.5 Cr (Rs.1 Cr monetary consideration and Rs. 4 Cr non-monetary consideration minus Rs. 1.5 Cr cost of acquisition).

Assume TDS rate is 20% total amount of tax to be deducted in the year III, year of chargeability, is Rs.70,00,000/. But there is no monetary consideration from which the tax to be deducted.

In order to resolve the issue, one may consider deduction of tax whenever monetary consideration is paid, despite the fact that deduction is not required to be done on strict reading of the Section 195. In the third year the eligible transferor pay the balance amount of tax Rs. 50,00,000/-(Rs. 70,00,000/- (Rs. 6,00,000+Rs.14,00,000) by way of advance tax.

Another Issue is, whether Form 15CB is required to be filed along with Form 15CA while remitting the amount to Non-resident though it is not taxed in India?

This matter is not free from doubt. Two views are possible. One view is that since the payment is not taxable at the time of remittance, no form 15CB is required though TDS deducted with abundant caution. According to the second view form 15CB required to be filed whenever TDS was made under the Act.
It is advisable to file form 27Q for deduction of tax made from the monetary consideration by the deductor.

GST Aspects:

The benefit of Section 45(5A) of Income Tax Act, 1961 comes with a rider that the eligible transferor should not part away with his share until the builder/developer obtains COC for the project.

The eligible transferor while choosing the option to avail the benefit under Section 45(5A) has also taken into consideration the impact under the GST laws on sale of his portion in the developed property.

Continuing with the above example, the eligible transferor obtains 10 flats in the developed property. For such supply of development and construction services, the builder/developer charges GST in accordance with the GST laws since such supply attracts the levy under GST laws[1] . As per the Joint development agreement, assuming, if the eligible transferor is liable to pay GST on such services to the builder/developer, then there will be an outflow of GST from the eligible transferor.

The eligible transferor can avail the same as input tax credit under GST laws and use the same against the GST payable when the eligible transferor sells his share of flats. However, the eligible transferor can avail the input tax credit only if the flats are sold prior to builder/developer obtaining COC.

If sale is happening after obtaining COC, then on such sale of flats, there would not be any levy of GST, since the same is treated as sale of immovable property under GST laws. Hence, the eligible transferor has to make a calculated decision as to whether the benefit under Section 45(5A) has to be availed or not. If the same is availed, he should be sure that either the joint development agreement pushes the GST liability on builder or prepare his mind to take the GST paid to builder/developer as cost.

Hence, it is advisable to take a holistic view before opting for the benefit enshrined in Section 45(5A) of Income Tax Act, 1961. No doubt, Section 45(5A) is a relief to the individuals or HUFs, however, one need to consider the potential loss under the GST laws for better tax planning.

[1]The author is of the view that there will be a liability on builder/developer on services provided to land owner even after the decision of Hyderabad CESTAT in the case of M/s Vasantha Green Projects v CCT, Rangareddy GST reported in 2018 (5) TMI 889. For the reasoning of the same, please read article in this journal)

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GST

ANALYSIS OF VASANTHA GREEN PROJECTS

Contributed by CA Sri Harsha & CA Manindar

The fate of indirect taxation in India, especially the taxation of services, is always like a rolling stone, which never gathers any moss. The positive list-based taxation was in vogue for certain period, and when the dust seems to be settled, the negative list-based taxation was introduced. When all the stake holders took a deep breath to unlearn the positive list-based taxation and learn the new law, then there was a repeal of negative list-based taxation and the introduction of goods and services tax law, more colloquially referred as GST.

Amidst the rapid changes of taxation of services, one sector which always felt the burnt of the changes is the real estate and construction sector. The development of law pertaining to this sector, if written goes into volumes. In this article, we are restricting ourselves only to analyse the recent decision of Vasantha Green Projects vs CCT, Rangareddy GST[1] which was delivered by Hyderabad CESTAT. The said decision deals with the limited issue of applicability of service tax on the construction services provided by the builder to the land owner in the context of joint development agreement.

Story So Far:

We will resume the analysis of the decision in subsequent paras. To appreciate the said decision, the story so far assumes importance. The Chennai CESTAT in the case of LCS City Makers Private Limited v Commissioner of Service Tax, Chennai[2] , has held that the builder has provided construction services to the land owners and accordingly liable to service tax. This was more clearly brought out in Para 12.5 of the said order:

"12.5 In the case of Land Owners also the UDS is registered in the name of the land owners. He parts with his rights in the land partially and receives a consideration for parting with such rights. The consideration is the form of constructed flats to be received later*. Of course, the constructed flat has got both value of material used and the value of service provided by the service provider. Obviously, service tax can be levied only on the value of service and cannot be equal to the full value of the land parted with by the land owner. This principle gets complied with when abatement from value of the constructed flat is given to the extent of 67% by Notification No. 1/2006-ST and earlier Notifications."*

(emphasis supplied)

The above judgment has created ripples in the industry because of the very reason that till such time, transaction between the builder and land owner was over looked by the authorities nor trade. At the same time, CBEC has released Circular No 151/2/2012-ST dated 10th Feb 2012, wherein it was stated that the transaction between the builder and land owner is a separate transaction and is subjected to tax and also laid down the valuation methodology and point of taxation as to when such service tax is to be paid by the builder on services provided to land owner. The valuation and point of taxation which were laid down by the Circular ibid, were being challenged before various forums but never was the existence of

[1] 2018 (5) TMI 889 – CESTAT Hyd

[2] 2012 (6) TMI 363 – CESTAT Chennai

liability was challenged. In other words, the trade has prepared for the payment of tax on the services provided to the land owners and was only disputing the value of tax and time of payment of tax.

In this background, the judgment issued by Honourable CESTAT of Hyderabad in case of Vasantha Green Projects (supra) sets the clock back to the square one, which is discussed in the following paras.

Decision of Vasantha Green Projects:

Before understanding the said decision, let us get the facts straight. Certain facts are evident from the certificate issued by Chartered Accountant which was relied in the judgment.

The said certificate states that Vasantha Green Projects has entered a joint develop agreement with land owners and obtained a General Power of Attorney to construct the residential villas/units and agreed to share 60 constructed villas & certain areas of constructed flats to the land owners on Barter system. The total number of villas are 197 with a total built up area of 9,30,116 Square feet out of which 60 villas having a built-up area of 2,71,268 has to be shared to the land owners. The balance 6,58,488 Square feet belongs to the developer. To arrive at the value of construction area of villas to be shared to land owners, the developer with the help of architect has arrived the cost of construction to be Rs 1,779/- per square feet. Hence, the total construction cost of villas pertaining to land owner's share is Rs 48,32,26,212/- (1,779/Sq feet * 2,71,268 Sq feet). The said cost was added to the construction cost of villas pertaining to the developer, on which the service tax was paid by the developer.

The said decision has stated that there is no requirement to see the transaction between the land owners and sale to ultimate customers as if there are two different transactions and essentially it is one transaction and the relevant para is reproduced hereunder for better understanding:

"5. We have considered the submissions made at length and perused the records as also the Board circulars and instructions in this regard. We find that in the present case, Revenue has demanded service tax from appellant on the ground that it was not paid correctly on the villas which were constructed by appellant for land owner, as a part of compliance of the agreement entered with the land owners. ***We find that adjudicating authority has confirmed the demands holding that transactions between builder and land owner and builder and buyers have to be understood as two separate transactions. It is undisputed that appellant has provided construction services to the land owner and as a consideration, received legal rights on his share of land, constructed Villas on that land and sold them, which would mean that appellant is investing the consideration received from first transaction of land owners right to construct in second transaction. In our view, merely because the consideration received from land owners is invested in construction of villas to other buyers on which service tax is paid, it cannot be concluded that service tax paid on consideration received from land owners has to be evaluated differently"***

(emphasis supplied)

Even though the para above states that developer has provided construction services to the land owner, goes forward to treat the consideration received from such transaction as an investment in the second transaction between the developers and ultimate customers and proceeds to state there is no requirement to pay tax on the services provided by developer to the land owner, because such consideration is invested in the second transaction. The order in another para states that there is no requirement to pay tax for the below stated reasons:

"7. It has to be construed, in the above factual matrix, ***that construction of villas for the land owners is a consideration towards the land on which villas were constructed and offered for sale to prospective customers. It would not be a rocket science to understand that the value which has been arrived at for sale of villas to prospective customers, would include the consideration paid or payable for acquisition of land. It is not a case that appellant has not discharged the service tax liability on the value received for the villas from prospective customers. In our view, if the consideration towards the acquisition of the land has been included in the value of the villas sold to prospective customers and appropriate service tax liability has been discharged the same value, it cannot be again made liable to service tax under the premise that sale value of the villas given to land owners is a consideration on which service tax liability was not discharged."***

However, what is not clear from the judgment is whether the developer is paying service tax on the entire value received from the ultimate customer or is he paying by applying abatement available. The logic of the order fails, if the developer is availing abatement because, once abatement is applied, it essentially takes out the value of land in the consideration received from the customer, which in the instant case would be the cost of construction of villas pertaining to land owners.

Let us take a small example, to understand the above. Let us say, the construction cost per sq feet of villa pertaining to land owners is Rs 2,000/-, which stands included in the cost of construction pertaining to the villas of developer, which is assumed to be Rs 6,000/-. When the developer applies an abatement of deemed 8% (75%-67%, where 67% is towards materials) on Rs 6,000/-, a portion of Rs 2,000/- would be gone from the tax net, whereas if the transaction between land owner and builder is made taxable, then tax should be charged @ 33% (after availing abatement of 67%, please note that abatement of 75% is not available since Rs 2,000/- is essentially cost of construction and not a value which includes the land). Then, how would one ensure that tax is paid on such amount and who would be responsible for payment of tax on such amounts. There will not be any change even if the tax rates prevalent during the period in dispute in the subject case are taken into consideration. The rate of tax applicable during the period in dispute is an abatement of 70% (if the value of land is included in the gross amount charged) and 60% (if the value of land is not included in the gross amount charged). Hence, there would be a difference of 10% instead of 8% as explained above.

Alternatively, one would argue that the abatement availed by the developer is towards the undivided share of land, however, the said argument fails on two counts, one being the developer has not invested a single rupee towards land and he claiming abatement towards the value of land, would be illogical and second being, the value of land is nothing but the construction cost of the villas of land owners and hence what is claimed as abatement is not the value of land but the construction cost of villas of the land owners.

However, if the entire value received from the customer is subjected to service tax without availing any abatement towards land, then the logic stated in the judgment holds good. However, the current judgment is not clear in the aspect whether the developer has paid service tax on the entire value without availing or availed abatement towards value of land. Hence, to this extent one has to carefully place reliance on the said judgment.

Further, even assuming that the developer has included the entire value of land in the construction cost of his share of villas, can that be a route to be out from the taxability of the transaction between the land owners and builders. Indirect tax being a transaction-based taxation, can it absolve the tax liability in the first transaction in a case consideration from first transaction is invested in the second transaction. If so, there should be a clear provision in the statute which would allow this. In our opinion, there is no such provision under the service tax law, which exempts the consideration received from first transaction from tax, if it is invested in the second transaction.

Further, when there is a separate agreement with the land owner with rights and obligations clearly being demarcated, can such a transaction be said to be as a part of the transaction which the developer enters into with the ultimate customer. The rights and obligations of development agreement and rights and obligations of agreement with customers are entirely different and it would be very hard to call it as a single transaction. Further, under the service tax regime, CBEC has clarified vide ______ that the sub-contractor is not absolved from payment of service tax on his services provided to main contractor for the reason that the main contractor pays service tax on the entire amounts received from the client/customer. Applying such circular, various CESTATs have passed orders stating that the sub-contractor has to pay service tax and main contractor has to claim the same as cenvat credit and use it while discharging his liability. The point, we wish to drive home is, when the law decides that the transaction of sub-contractor and main contractor as different transaction from the transaction of main contractor and client/customer, which is essentially a single activity, the view taken in this judgment treating the transaction of land owner and developer and developer and customer as a single transaction is hard to digest. We have to wait and see whether it passes the test at higher forums.

Apart from the above observation, the judgment also tries to distinguish the ratio of LCS City Makers (supra). The relevant para of the judgment is hereunder:

13. The reliance placed by Ld. DR on the case of LCS City Makers Pvt. Ltd. will also not carry the case of Revenue any further, as in that Bench upheld the contention of the Revenue that recording that ***"the facts and circumstances of the case do not warrant assessment of a different value for services in respect of flats sold to individual buyers as compared to flat handed over to the land owners";*** *and recorded* ***that the flats which were allotted to land owners were sold by land owners. In the case in hand, the facts are different.***

(emphasis supplied)

From the above para, it is evident that the Vasantha Green Projects judgment tries to make a distinction from LCS City Makers, by stating that in case of LCS City Makers, the flats were sold by land owners, wherein the case of Vasantha Green Projects, they were retained by land owners and not sold by them.

We opine that the above distinction requires reconsideration since, there could not be any difference in taxation at developer's level if the flats/villas are sold or retained by the land owners. The taxation at developer's level should remain either exempted or taxable irrespective of the fact the land ownersretains or sells his share.

Further, there would be every possibility that the builder/developer might sell some flats after obtaining completion certificate (depending upon the market conditions). In such cases, where flats are sold after obtaining completion certificate, then there is no requirement to charge GST in light of Schedule III of CGST Act, 17. In such cases, the construction cost incurred towards the land owner share of flats/villas will not be subjected to GST in the hands of developer/builder, since such flats/villas are sold after obtaining completion certificate and the judgment does not address such instances.

In light of the above issues, we opine that the above judgment requires reconsideration and cannot be relied upon without considering the facts under which the judgment is proposed to be applied.

GST

SUMMARY OF AAR IN ACRYMOLD

Contributed by CA Manindar & Bhavani

Sl. No	**GST-ARA-12/2017/B-15**
Name of Ruling	Acrymold
TMI Citation	2018 (5) TMI 597 - AUTHORITY FOR ADVANCE RULINGS MAHARASHTRA
AAR State	MAHARASHTRA
Macro Issue	The issue is regarding classification of trophies and awards made of different material viz. Metal, Plastic, Glass, MDF/Wood, Resin etc and the questions raised before advance authority are as follows: 1. If the word TROPHY is specifically mentioned under 83062920 (Article of Base Metal), So can all trophies made of any material be classified under this HSN? 2. If different HSN codesare to allocated to trophies assembled of different material and if there is a combination of different materials and about 75% (value terms) is getting used of any one raw material, under which HSN code, they should be classified?
Facts	Applicant is engaged as an Importer, Manufacturer and Trader of Trophies and Gifts made of different material (including their combinations) viz. Metal, Plastic, Glass, MDF/Wood, Resin etc.
Applicant Stand	As per the CBEC site and other official documents the above product is classified under the HSN 83062920. The chapter no. 83 deals specifically with articles of BASE METAL. As Trophies and Awards are made of a variety of material namely METAL, PLASTIC, GLASS, MDF/WOOD, RESIN etc. There is no clear classification of the same under other chapters. As per Customs Classification, there is discrepancy of HSN allotted to these goods which are imported under different HSN code for this same product viz-a viz Mumbai, Kolkata & Delhi ports leading to variation in IGST rate for the same product.
Department Stand	**Question 1: If the word TROPHY is specifically mentioned under 83062920, So can we sell all trophies made of any material under this HSN?** Chapter 83 specifically deals with **"Miscellaneous articles of base metal"**. A base metal is a common and inexpensive metal, as opposed to a precious metal such as gold or silver. It includes trophies of base metals and not of any other material. The Tariff item 83062120 covers "Trophies". The mere mention of the word "trophies" would not mean that trophies of any material would be covered by the heading. Base metal articles containing two or more base metals are classified as articles of that metal which **predominates by weight** over each of the other metals, except where the headings otherwise require (e.g., copper- headed iron or steel nails are classified in heading 74.15 even if the copper is not the major constituent).

The same rule applies to articles made partly of non-metals, provided that, under the General Interpretative Rules, the base metal gives them their **essential character.**
The expression "base metals" means iron and steel, copper, nickel, aluminium, lead, zinc, tin, tungsten (wolfram), molybdenum, tantalum, magnesium, cobalt, bismuth, cadmium, titanium, zirconium, antimony, manganese, beryllium, chromium, germanium, vanadium, gallium, hafnium, indium, niobium (columbium), rhenium and thallium.

Any reference to a base metal in Chapters 72 to 76 and 78 to 81 or elsewhere in the nomenclature also includes the alloys of that metal.
Explanations:
(1) **Alloys of base metals with precious metals:** These alloys are classified as base metals provided that no one of the precious metals (silver, gold and platinum) constitutes as much as 2% by weight of the alloy. Other alloys of base metals with precious metals are classified in Chapter 71.
(2) Alloys of base metals: These alloys are classified with the metal which predominates by weight, with the exception of ferro-alloys (see the Explanatory Note to heading 72.02) and master alloys of copper (see the Explanatory Note to heading 74.05)
(3) Alloys of base metals of this Section with non-metals or with the metals of heading 28.05: These are classified as alloys of base metals of this Section provided the total weight of base metals of this Section equals or exceeds the total weight of the Other elements present. If this not the Case, the alloys are generally Classified in heading 38.24.

Even though the word TROPHY is specifically mentioned under 83062920, all trophies made of any material cannot be classified under this HSN and are to be classified as per the below applicable provisions of the Customs Tariff Headings by applying the principal of specific over general

Description of materials	Description as per HSN	HSN Code	GST Rate
For Glass Crystal Trophies & Awards	Other	70181090	18%
For Plastic Trophy and trophy parts	Others	39261019	18%
For Wooden Trophies & Frames	Wooden frames for paintings, photographs, mirrors or similar objects	4414	18%
For Metal Trophies & Awards	Trophies	83062920	12%
	Others	83062990	
	Photograph, picture or similar frames	83063000	
For Trophies made of pop and other Resins	Articles of Plaster or of compositions based on plaster	6809	18%
	Other articles	68099000	

Question 2: If different HSN codes are to allocated to trophies assembled of different material and if there is a combination of different materials and about 75% (value terms) is getting used of any one raw material, under which HSN code, they should be classified?

The HSN Notes to Heading 8306 say thus -
(B) Statuettes and Other ornaments
This group comprises a wide range of ornaments of base metal (whether or not incorporating subsidiary non-metallic parts) of a kind designed essentially for decoration.
The group covers articles which have no utility value but are wholly ornamental, and articles whose only usefulness is to contain or support other decorative articles or to add to their decorative effect.

By application of rule 2(b) of General Rules for Interpretation of Tariff, goods which are classifiable under two or more headings, classification shall be effected as follows:
(a) The heading which provides the **most specific description shall be preferred to headings providing a more general description.** However. when two or more headings each refer to part only of the materials or substances contained in mixed or composite goods or to part only of the items in a set put up for retail sale, those headings are to be regarded as equally specific in relation to those goods. even if one of them gives a more complete or precise description of the goods.
(b) Mixtures, **composite goods** consisting of different materials or made up of different components, and goods put up in sets for retail sale, which cannot be classified by reference to (a), shall be classified as if they consisted of the material or **component which gives them their essential** character, in so far as this criterion is applicable.
(c) When goods **cannot be classified by reference to (a) or (b)**, they shall be classified under the heading which **occurs last in numerical order among those which equally merit consideration.**

Goods which cannot be classified in accordance with the above rules shall be classified under the heading appropriate to the goods to which they are most akin.

Classification of Composite article: Articles of base metal (including articles of mixed materials treated as articles of base metal under the Interpretive Rules) containing two or more base metals are to be treated as articles of the base metal predominating by weight over each of the other metals.

For this purpose:
(a) iron and steel, or different kinds of iron or steel, are regarded as one and the same metal:
(b) an alloy is regarded as being entirely composed of that metal as an alloy of which, by virtue of Note 5, it is classified; and
(c) a cermet of heading 8113 is regarded as a single base metal.

Ruling with reasons	Q1. If the word TROPHY is specifically mentioned under 83062920, So can all trophies made of any material can be classified under this HSN? A1. Answered in the negative. Trophies made of other than base metal can be classified under those HSN Tariff headings that covers the respective material. Q.2 If different code is allocated to trophies assembled of different material, I would like to know if there is a combination of different materials and about 75% (value terms) is getting used of any one Raw Material, under which HSN should we make bill? A2. The question is of a general nature. In absence of the needful information as to the constituent materials of the trophies, the question was not answered.
Discussion Outcome	1. The decision clarifies the legal position that though there is a specific word 'Trophy' under 83062920, the said classification can only be adopted in case the trophy is made of base metals as the respective chapter covers articles of base metals. 2. In case of trophy made of material different from that of base metal, then such trophy cannot be classified under 83062920. They should be classified under the Tariff headings (as listed above) that covers the respective material. 3. In case of trophies made by using two or more material, the AAR has not conclusively answered the question on the reasoning that the question involved is a general one. However, it was mentioned that classification in such cases can be adopted on the basis of General Rules for Interpretation of Tariff. 4. According to Rule 3(b) of General Rules for Interpretation of Tariff, in case of goods made of different material, then they shall be classified as if they consisted of the material or component which gives them their essential character. Thus, if a trophy is made of base metal (bronze) with wooden base, then it can be said that trophy is made of two or more materials. Out of which, base metal (bronze) will be the essential character as the trophy is still considered as made bronze. In such case, the said shall be classified as if it is made of base metal (bronze) alone under 830629290.

This article is contributed by CA Manindar K Partners of SBS and Company LLP, Chartered Accountants.
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GST

SUMMARY OF AAR IN HAFELE INDIA PRIVATE LIMITED

Contributed by CA Manindar & Bhavani

<table>
<tr><td>Sl. No</td><td>GST-ARA-10/2017/B-13</td></tr>
<tr><td>Name of Ruling</td><td>HAFELE INDIA PRIVATE LIMITED</td></tr>
<tr><td>TMI Citation</td><td>2018 (5) TMI 646 - AUTHORITY FOR ADVANCE RULING - MAHARASHTRA</td></tr>
<tr><td>AAR State</td><td>MAHARASHTRA</td></tr>
<tr><td>Macro Issue</td><td>Whether the product "Caesarstone" imported by the applicant can be classified under HSN Code 2506 or 6810?</td></tr>
<tr><td>Facts</td><td>The applicant is engaged in importation of Bathroom and Kitchenware fitting and Caesarstone Quartz. At the time of importation of Caesarstone Quartz, it is liable to pay Basic Customs Duty and IGST and classified under heading 6810. For outward supply of goods, it is liable to pay GST and there arises the question of whether it is to be classified under heading 2506 or 6810.

<table>
<tr><th><u>Sr No</u></th><th><u>HSN Code</u></th><th><u>Description</u></th><th><u>IGST Rate</u></th></tr>
<tr><td>1.</td><td>2506</td><td>Quartz (other than natural sands) quartzite, whether or not roughly trimmed or merely cut by sawing or otherwise in to blocks or slabs of a rectangular (including square) shape</td><td>5%</td></tr>
<tr><td>2.</td><td>6810</td><td>Articles of cement of concrete or of artificial stone whether or not reinforces</td><td>15%</td></tr>
</table></td></tr>
<tr><td>Applicant Stand</td><td>Guiding Principles involved to settle the issue:
1. Classification of good under Customs Tariff Act 1975 along with relevant chapter notes of Chapter 25 and 68
2. General Rules of interpretation of the first schedule to the Customs Tariff Act 1975
3. HSN explanatory notes released by WCO

<u>Whether the good fits under Heading 2506</u>

Quartz is combined with polymers and pigments and compacted under intense vacuum and cut into slabs to for the output -ceasarstone.

The Chapter Note 1 of Chapter 25 clearly states that “------, <u>the headings of this Chapter cover only products which are in the crude state or which have been washed</u>(even with chemical substancese liminating the impurities without changing the structure of the</td></tr>
</table>

	product), crushed, ground, powdered, levigated, sifted, screened, concentrated by flotation, magnetic separation or **other mechanical or physical processes** (except crystallization), *but not products that have been roasted, calcined, obtained by mixing or subjected to processing beyond that mentioned in each heading."* It is imperative to understand that the composition of Caesarstone contains 93% crushed quartz. Quartz is combined with high-quality polyester resins and pigments and is then compacted under intense vacuum and pressure into dense and non-porous slabs. As per Chapter Note I to Chapter 68 which clearly provides that chapter does not cover goods falling under Chapter 25. As the manufacturing process is covered under the mechanical process and considering Rule 2(a) and Rule 3(b) of General Rules for Interpretation and Chapter Note 1 to Chapter 25, Caesarstone imported shall be construed as a Quartz and classified under chapter 25.
Department Stand	By considering the content of Chapter Note 1 to Chapter 25, the goods should not change the character of mineral product. In addition to mechanical and physical process, chemical process is also involved. Such process carried out is beyond the scope of Chapter Note 1 to Chapter 25. Caesarstone is an engineered quartz surface and it is a man made stone or artificial stone. Quartz is one of the raw material to produce Caesarstone and addition of polymer resins and pigments to the quartz changes the character/structure of mineral product. AA also considereda ruling of Harmonised Tariff Schedule of United States in case of Silestone TM wherein the slabs composed of 93% Quartz and 7% of resin binder, it is classified under sub heading 6810.99.00 and considered as artificial stone.
Ruling with reasons	Caesarstone imported by the applicant is to be classified under HSN code 6810
Discussion Outcome	On perusal of the Tariff headings of Chapter 25 and Chapter 68, it is clearly evident that a processed stone (artificial or natural) will be classifiable under chapter 68 while chapter 25 covers only natural stones in crude state. Accordingly, no contrary views have been shared.

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AUDIT

IND AS 115 - REVENUE FROM CONTRACTS

Contributed by CA Sandeep Das

The Ministry of Corporate Affairs (MCA), on 28 March 2018, notified Ind AS 115, Revenue from Contracts with Customers (which is based on IFRS 15, Revenue from Contracts with Customers) as part of the Companies (Indian Accounting Standards) Amendment Rules, 2018.

The new standard is effective for accounting periods beginning on or after 1 April 2018, thus aligning the Ind AS 115 applicability date with the IFRS applicability date i.e. 1 January 2018.

Ind AS 115 replaces existing revenue recognition standards Ind AS 11, Construction Contracts and Ind AS 18, Revenue and revised guidance note of the Institute of Chartered Accountants of India (ICAI) on Accounting for Real Estate Transactions for Ind AS entities issued in 2016.

The new standard also modifies other Ind AS for e.g. Ind AS 16, *Property, Plant and Equipment* for determining the date of sale of Property, Plant and Equipment (PPE) i.e. date of disposal of an item of PPE is the date the recipient obtains control of that item in accordance with Ind AS 115.

Scope of IND AS 115

The new standard applies to contracts with customers to deliver goods or services, except when those contracts are for:

- Lease contracts under Ind AS 17, Leases
- Insurance contracts under Ind AS 104, Insurance contracts
- Rights or obligations that are in the scope of certain financial instrument guidance for example IND AS 109
- Non-monetary exchanges between entities in the same line of business which facilitates sales to customers other than parties to the exchange.

Fundamental principle of Ind AS 115

The fundamental principle of the new standard is that revenue should be when an entity transfers controls of goods or services to a customer at the amount to which the entity expects to be entitled. To achieve the core principle, the new standard establishes a five – step model framework that entities would need to apply to determine when to recognize revenue and amount. The new approach is likely to bring significant changes in the way companies recognize, present, and disclose their revenue.

- Step I - Identify the contract with Customer.
- Step II - Identify performance obligation in the contract
- Step III – determine the transaction price
- Step IV- Allocate the transaction price to the performance obligation
- Step V - Recognize revenue when the entity satisfies its performance obligations

The underlying assumptions is transfer of risk and rewards model to a five-step approach which primarily focuses on transfer of control of goods and services by an entity under a contract with its customers.

Step I - Identify the contract with the customer

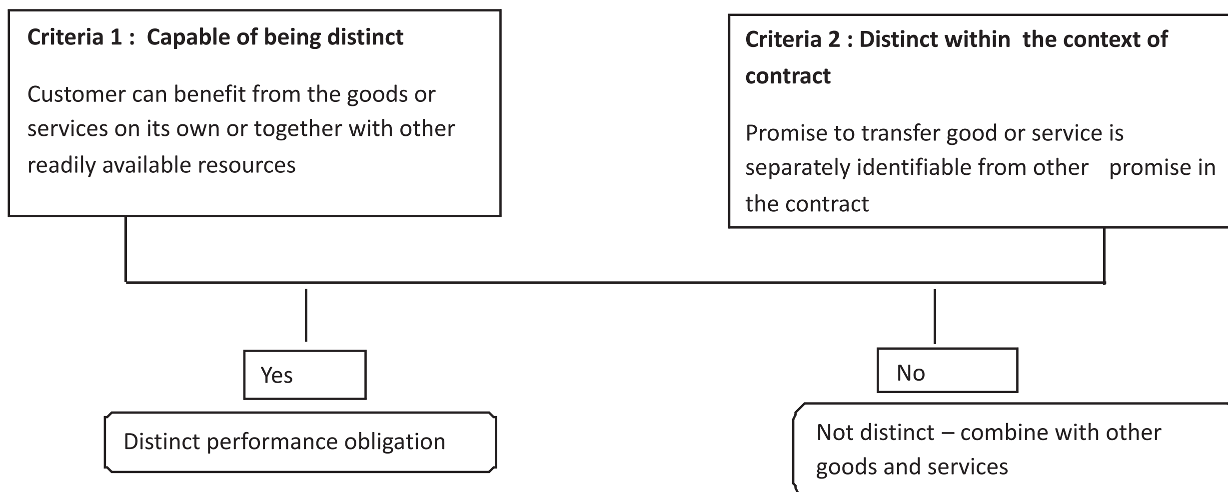
The new standard defines a"Contract" as an agreement between two or more parties that creates enforceable rights and obligations and specifies that enforce ability is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices.

Contract with a customer exists when it meets all of the following criteria.

- Collection of consideration is considered as probable.
- There is a commercial substance.
- Right to goods or services and payment terms can be identified
- It's approved and the parties are committed to their obligations.

Step II – Identify the performance obligations

The new standard requires an entity to identify the performance obligations. Promise to deliver goods or provide a service in a contract with a customer constitutes a performance obligation if the promised good or service is distinct.
A promised good or service is distinct from other goods and services in the contract if meets two criteria.



Step III – determine the transaction price

Ind AS 115 requires an entity to consider the terms of the contract and its customary business practices to determine the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

Following factors shall be considered when determining transaction price:

- If the consideration includes variable amount, an entity should estimate the amount of consideration to which it will be entitled in exchange for transferring the promised goods or services to a customer.

- In determining the transaction price, an entity should adjust the promised amount of consideration for the time value of money if significant financing component exist.

- Non cash consideration is measured at fair value, if that can be reasonably estimated.

- Entities need to determine whether consideration payable to a customer represents a reduction of the transaction price, a payment for a distinct goods or service, or a combine of the two.

Step IV - Allocating the transaction price

Under Ind AS 115, entities are required to allocate the transaction price to each performance obligation in proportion to its stand-alone selling price i.e. the price at which an entity would sell the promised good or service separately to customer.

The best evidence of the stand -alone selling price is an observable price from stand -alone sales of that goods or service to similarly situated customers. Entity shall estimate the stand-alone selling price using the following methods:

- Expected cost plus marging approach
- Residual approach
- Adjusted market assessment approach

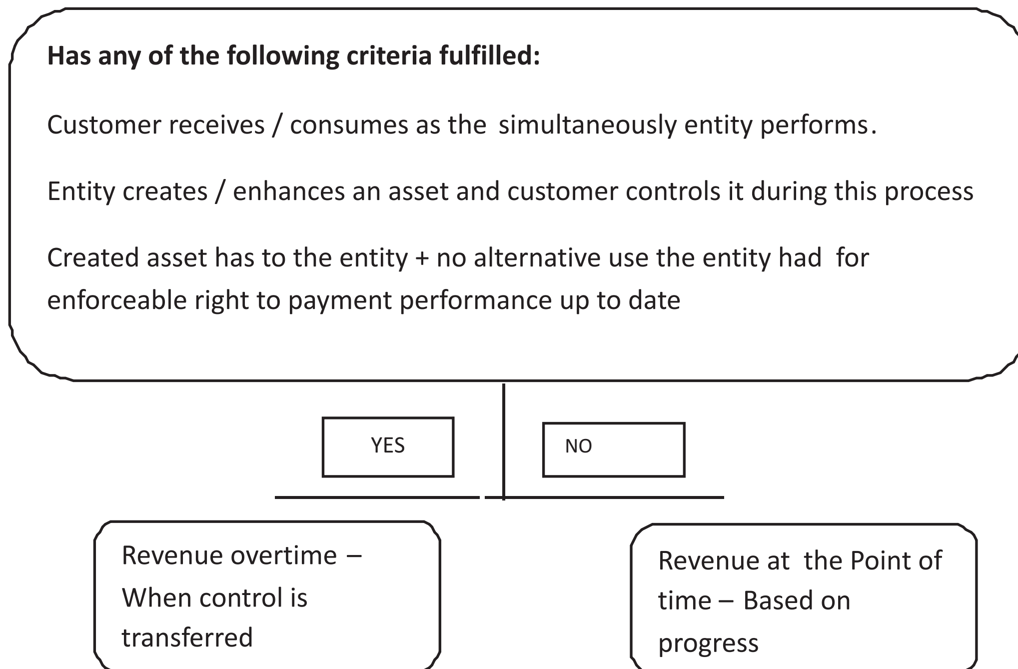
Step V - Recognise revenue

Revenue may be recognized either at a point in time or over a period of time. For the purpose of standard, control refers to the customers ability to direct the use of and obtain necessary benefits from the asset.

An entity would have to determine at contract inception whether it satisfies the performance obligation over time or at a point in time.

At the end of each reporting period, for each performance obligation satisfied over time, revenue should be recognized by measuring the progress towards complete satisfaction of that performance obligation. An entity should use a single method consistently for such measurement. Ind AS 115 specifies two types of methods: input method and output method, which an entity should consider based on the nature of the goods or services. The objective is to use a method which depicts the transfer of control of goods or services to the customer.

When to recognize revenue:



Key Challenges for Industries

- The revenue and profit recognition will change for some entities and they will need to consider
- whether revenue should be recognised over time or at a point in time
- how shipping term will change the timing of recognition
- the extent to which distinct goods or services are supplied, which should be accounted for separately
- whether costs relating to obtaining a contract must be capitalised
- whether revenue must be adjusted for the effects of the time value of money
- how to account for contract modifications
- the impact of new guidance where pricing mechanisms include variable amounts
- whether accounting treatment will be changed for different types of licenses and royalties
- accounting for warranty covers given to customers

Other Issues :

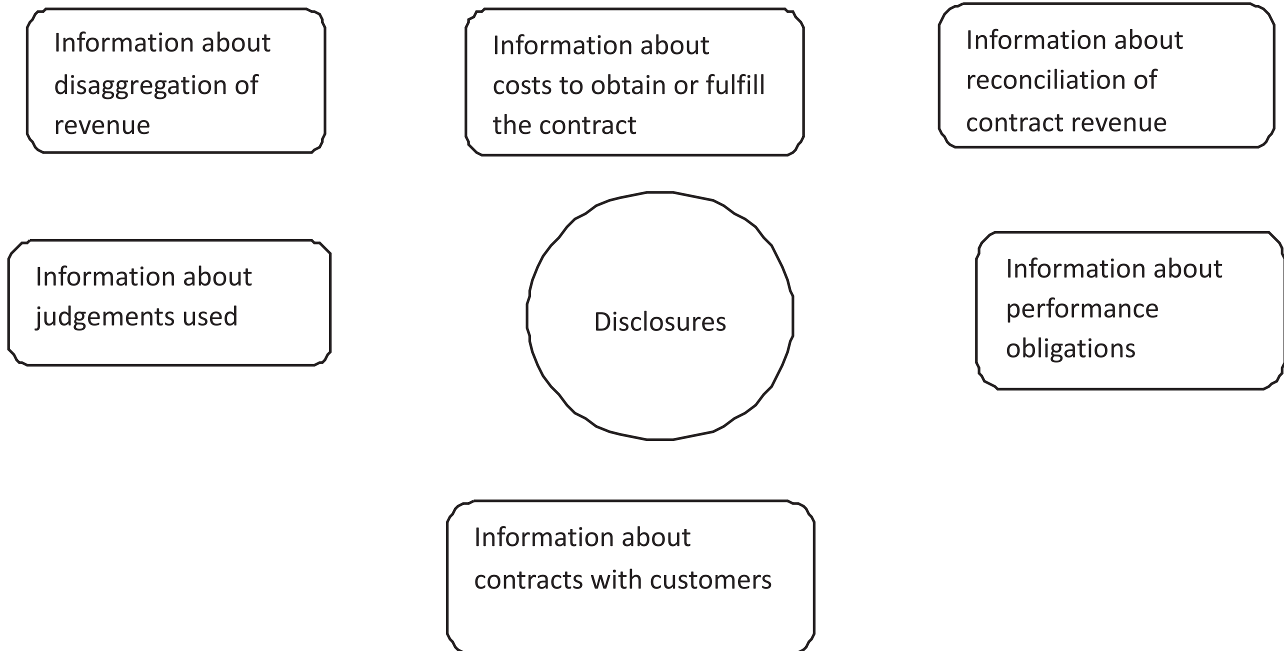
- The accounting for contract modifications is complex and differs significantly depending on whether a new performance obligation is created and, on the pricing

- Revenues from manufactured goods may historically have been recognized on delivery to the customer. Now, if the contract meets the 'over time' test, then the revenue would be recognized as the manufacturing happens – like current longterm contract accounting.

- Cash incentives and incentives to provide free or discounted goods can be separate performance obligations rather than marketing incentives

- Non-performance penalties (e.g. for failure to meet service level agreements) will generally need to be deducted from revenue rather than charged as an expense

Disclosure Requirementsa



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