

Point of taxing Krishi Kalyan Cess - A debacle

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"We legislate first and think afterwards. Complicity is heaped upon complexity and confusion becomes worse confounded"

- *Nanabhoy Ardeshir Palkhivala*

The power to levy and collect taxes comes from the Constitution of India ('Constitution'). Article 246 of the Constitution empowers both the Parliament and the State Legislature to make laws with respect to the matters specified in VII Schedule, viz. Union List, State List and Concurrent List.

The fiscal wisdom mandates that all taxes should be levied and thus, all fiscal legislations including their amendments are prospective in nature. In extra ordinary situations like tax being strike down by Courts due to legislative defects etc., the law makers depart from this fundamental principle and impose tax retrospectively.

Under the Indirect Tax laws, the charge of tax is on the occurrence of an event. For example, excise duty is levied on 'manufacture or production', sales tax on 'sale', and customs duty on 'import' and 'export' of goods. In case of services, the taxable event is 'provision of service'. No tax can be levied in the absence of taxable event. Also, being an Indirect Tax, the taxpayer ordinarily collects tax from the customer.

When the whole country is eagerly awaiting the Goods & Service Tax to see light of the day, the government has introduced Krishi Kalyan Cess (effective from June 1, 2016) ('KKC'). KKC has not only been introduced by the government in a perfunctory manner but the same seemed to have retrospective applicability. Simply put, KKC seems to have been applied even on services wherein the taxable event occurred prior to June 1, 2016.

Rule 5 of Point of Taxation Rules, 2011 ('POTR') deals with non-applicability of service tax in situations where the service provider receives consideration before imposition of service tax on new service and raises invoice before imposition or within 14 days of imposition.

Vide Notification No.10/2016-ST dated March 1, 2016, Rule 5 of POTR has been made applicable in case of new levies like KKC. Consequently, KKC is applicable in situations where the service has been provided before June 1, 2016 and invoice is raised by June 14, 2016 but payment is received post June 1, 2016. It is pertinent to note that point of taxation for such services would have already occurred earlier under Rule 3 of POTR (viz. date of invoice). The aforesaid amendment in Rule 5 of POTR results in levy of KKC from retrospective effect

when the charging provision (*viz.* Section 161 of the Finance Act, 2016) through which KKC is levied, never intended to make this cess applicable retrospectively.

This anomaly raises a fundamental question as to whether POTR envisage or can legally determine more than one point of taxation for a particular service.

Taking note of the anomaly and the unrest prevailing in the industry, the Central Government has now issued Notification No.35/2016-ST dated June 23, 2016 ('Notification'). The Notification exempts KKC where the service was provided and invoice was issued prior to June 1, 2016 though payment was received thereafter.

Though the Notification seems to have been issued with a noble intent, it raises a fundamental issue as to whether it has retrospective implication and exempt transactions prior to its issuance namely for the period till June 22, 2016. This is due to the reason that the Finance Act, 1994 does not empower the Central Government to issue exemption notifications with retrospective effect.

Both the Notification and Central Government are also silent on the fate of KKC already paid by taxpayers prior to issuance of this Notification (*viz.* till June 22, 2016). The only legal remedy available to the taxpayer seems to seek refund of KKC from the government if it has not collected KKC from its client else the client has to seek refund.

The next pertinent question which merit consideration is - was this Notification really required. Even if the Central Government had not issued this Notification, the taxpayers would have challenged newly inserted Explanations to Rule 5 of POTR on the ground of creating a retrospective levy of KKC which has not at all been contemplated under the charging provision (*viz.* Section 161 of the Finance Act, 2016). Rule 5 of the POTR is only a machinery provision to effectuate the levy and in no manner, cannot override the charging provision.

The Central Government has increased rate of service tax several times in the past or imposed Cess like Swachh Bharat Cess. The Government has ample experience to visualise challenges and issues faced by Industry in such transition.

The manner in which the Central Government has brought in the levy of KKC, is unfortunate. On May 26, 2016, the Central Government issued series of Notifications to bring the levy in force. It was 23 days after the levy was brought into force, the Government issued the instant Notification. It is not unreasonable to expect the Government to come up with all Notifications in one go and in a reasonable period before the introduction of levy. The certainty in taxation is the most reasonable and legitimate expectation that a taxpayer can have from the Exchequer. We hope the Government acts in a mature and reasonable manner in future especially at the time of introduction of GST.