

**F. No. B1/16/2007-TRU**  
**Government of India**  
**Ministry of Finance**  
**Department of Revenue**  
**Tax Research Unit**  
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**New Delhi, the 22<sup>nd</sup> May, 2007**

To,

Director General (All)  
Chief Commissioner of Central Excise (All)  
Chief Commissioner of Central Excise & Customs (All)  
Commissioners of Service Tax (All)  
Commissioners of Central Excise & Customs (All)

Madam / Sir,

Subject: Post Budget 2007-08 notifications to give effect to the provisions of the Finance Act, 2007 - regarding.

The Finance Bill, 2007 received the assent of the President of India on the 11<sup>th</sup> May, 2007 and the corresponding Act is published in the Gazette of India dated 12<sup>th</sup> May, 2007 as Act No.22 of 2007.

2. Certain provisions relating to the levy of service tax in the Finance Act, 2007 shall come into force from a date to be notified. For this purpose, notifications No.23/2007 to 32/2007-Service Tax, all dated 22<sup>nd</sup> May, 2007 have been issued.

3. Seven services which are specifically mentioned in the category of taxable services and amendments made relating to existing taxable services shall come into effect from the 1<sup>st</sup> June, 2007. In other words, changes made in the Budget 2007-08 relating to scope and coverage of taxable services will be effective from 01.06.07 [Notification No.23/2007-Service Tax dated 22.05.07].

4. Section 65 defines taxable services and various terms used in relation to taxable services. Section 66 is the charging section and provides for levy of service tax on taxable services. These two sections have been amended in the Finance Act, 2007 and these amendments shall come into effect from 01.06.07 [Notification No.23/2007-Service Tax dated 22.05.07].

5. Seven services which are specifically mentioned in the category of taxable services are:

- (i) Service provided by a telegraph authority in relation to telecommunication service [sub-clause (zzzx) of section 65(105)];
- (ii) Service provided in relation to mining of mineral, oil or gas [sub-clause (zzzy) of section 65(105)];
- (iii) Service provided in relation to renting of immovable property for use in the course or furtherance of business or commerce [sub-clause (zzzz) of section 65(105)];
- (iv) Service provided in relation to the execution of a works contract [sub-clause (zzzza) of section 65(105)];
- (v) Service provided in relation to development and supply of content for use in telecom services, advertising agency services and on-line information and database access or retrieval services [sub-clause (zzzzb) of section 65(105)];
- (vi) Service provided by any person, except a banking company or a financial institution including a non-banking financial company or any other body corporate or commercial concern, in relation to asset management including portfolio

- management and all forms of fund management [sub-clause (zzzzc) of section 65(105)]; and
- (vii) Service provided in relation to design services [sub-clause (zzzzd) of section 65(105)].
6. Following amendments have been made relating to existing taxable services:
- (i) Exclusion of business directories, yellow pages and trade catalogues which are primarily meant for commercial purposes from the scope of the definition of “Book” under sale of space or time for advertisement service [section 65(105)(zzzm)];
  - (ii) Inclusion of motor vehicles capable of carrying more than twelve passengers for hire or reward, other than such motor vehicle and maxicab rented to an educational body, imparting skill or knowledge or lessons on any subject or field, other than a commercial training or coaching centre, within the definition of “cab” under rent-a-cab service [Section 65(20)];
  - (iii) Insertion of explanation under mandap keeper service [section 65(66) and 65(67)] and pandal or shamiana contractor service [section 65(77a)] stating that social function appearing in these two taxable services includes marriage functions also;
  - (iv) Inclusion of marriage event within the scope of event management service [section 65(40)];
  - (v) Insertion of explanation under manpower recruitment or supply service [section 65(105)(k)] to clarify that manpower recruitment or supply agency service includes services in relation to pre-recruitment screening, verifying the credentials of the candidate, authenticity of documents submitted by the candidates and verification of antecedents;
  - (vi) Banking and other financial services:
    - a. Substitution of the words “any other person” with “commercial concern” in the definition of taxable service of banking and other financial services [section 65(105)(zm)] and also in the definition of banking and other financial services [section 65(12)],
    - b. Inclusion of cash management services within the scope by deleting the specific exclusion [section 65(12)], and
    - c. Insertion of explanation to explain the term “financial leasing” [section 65(12)];
  - (vii) Renaming of management consultant’s service as management or business consultant’s service [section 65(105)(r)], and inclusion of business consultancy in the definition itself [section 65(65)];
  - (viii) Inclusion of exclusion of computer hardware engineering consultancy under consulting engineer service by deleting the specific exclusion [section 65(105)(g)];
  - (ix) Clarification that “goods” for the purposes of this service includes computer software under management, maintenance or repair service [section 65(64)].

Amendment to Rules:

7. In view of the merger of various telecommunication related taxable services into “telecommunication service”, notification no. 36/2004-Service Tax dated 31.12.04 and Rule 2(1)(d)(i) of the Service Tax Rules, 1994 have been amended so as to substitute the reference to various telecommunication related taxable services, namely telephone connection, pager, leased circuit, communication through telegraph, communication through telex and facsimile communication, with the merged “telecommunication service” [Notification No.27/2007-Service Tax dated 22.05.07 & Notification No.28/2007-Service Tax dated 22.05.07]. Amendment is consequential.

7.1 Export of Services Rules, 2005 and the Taxation of Services (Provided from Outside India and Received in India) Rules, 2006 have been amended so as to categorise the newly specified taxable services under Rule 3 [Notification No.30/2007-Service Tax dated 22.05.07&

Notification No.31/2007-Service Tax dated 22.05.07]. Taxable services have been categorised as under:

Sr. No.	Name of Taxable Service	Sub-clause of section 65(105)	Export of Services Rules, 2005	Taxation of Services (Provided from Outside India and Received in India) Rules, 2006
1.	Telecommunication service	zzzx	Category 3 [Rule 3(1)(iii)]	Category 3 [Rule 3(iii)]
2.	Mining of mineral, oil or gas	zzzy	Category 1 [Rule 3(1)(i)]	Category 1 [Rule 3(i)]
3.	Renting of immovable property	zzzz	Category 1 [Rule 3(1)(i)]	Category 1 [Rule 3(i)]
4.	Works contract service	zzzza	Category 1 [Rule 3(1)(i)]	Category 1 [Rule 3(i)]
5.	Development and supply of content	zzzzb	Category 3 [Rule 3(1)(iii)]	Category 3 [Rule 3(iii)]
6.	Asset management	zzzzc	Category 3 [Rule 3(1)(iii)]	Category 3 [Rule 3(iii)]
7.	Design services	zzzzd	Category 3 [Rule 3(1)(iii)]	Category 3 [Rule 3(iii)]

Exemption from service tax:

8. Notification No.24/2007-Service Tax, dated 22.05.07 exempts taxable service provided by any person in relation to renting of immovable property from service tax equivalent to service tax payable on the amount of property tax, actually paid by the service provider to the local authority. In other words, service tax is payable on the rental amount received less the actual amount of property tax paid.

8.1 However, any amount such as interest, penalty paid to the local authority by the service provider on account of delayed payment of property tax or any other reasons can not be treated as property tax for the purpose of this exemption and hence, deduction of such amount from the gross amount charged shall not be allowed.

8.2 If property tax is paid for a period which is different from the rental period, property tax proportionate to the rental period shall be calculated and the amount so calculated shall be excluded from the rental amount received for the purpose of levy of service tax.

8.3 There may be a situation where property tax is paid after the payment of service tax on the rental. As a result, deduction of property tax paid from rental could not be availed of at the time of payment of service tax. In such cases, Rule 4C of the Service Tax Rules, 1994 provides self-adjustment of excess service tax paid without any limit [Notification No.24/2007-Service Tax, dated 22.05.07].

8.4 Construction of ports is specifically exempted from levy of service tax under commercial or industrial construction service [section 65(25b)] vide notification No.16/2005-Service Tax, dated 07.06.05. Construction of ports under the newly introduced commercial or industrial construction service provided in relation to the execution of works contract under section 65(105)(zzzza) has also been exempted. Accordingly, notification No.16/2005-Service Tax, dated 07.06.05 has been rescinded and a combined notification No.25/2007-Service Tax dated 22.05.07 has been issued exempting commercial or industrial construction service, and services provided in relation to the execution of works contract, provided to any person by any other person in relation to construction of a port or other port. However, services such as completion and finishing, repair, alteration, renovation, restoration, maintenance or repair provided in relation

to existing port or other port shall be outside the scope of this exemption and hence, leviable to service tax.

Optional Composition Scheme for Works Contract:

9. Services provided in relation to the execution of a works contract [section 65(105) (zzzza)] is a taxable service. Works contract for the purposes of levy of service tax has been defined to mean a contract wherein:

- (i) transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods, and
- (ii) such contract is for the purposes of carrying out, -
  - (a) erection, commissioning or installation,
  - (b) commercial or residential construction and related completion and finishing services, and
  - (c) turnkey projects including engineering, procurement and construction or commissioning (EPC) projects.

9.1 Works contract is a composite contract for supply of goods and services. A composite works contract is vivisected and,-

- (i) VAT / sales tax is leviable on transfer of property in goods involved in the execution of works contract [Art.366(29A)(b) of the Constitution of India], and
- (ii) service tax will be leviable on services provided in relation to the execution of works contract.

9.2 Service tax is chargeable on the gross amount charged by the service provider for the taxable services provided (section 67). In the case of works contract, the taxable value of services is to be determined by vivisecting the composite works contract. Rule 2A of Service Tax (Determination of Value) Rules, 2006 [Notification No.29/2007-Service Tax dated 22.05.07], provides that value of works contract service shall be equivalent to the gross amount charged for the works contract less the value of transfer of property in goods involved in the execution of the said works contract. Thus, wherever the service provider maintains records, the value of services shall be the gross amount charged for the works contract less the value of transfer of property in goods involved in the execution of the works contract.

9.3 Wherever VAT/ sales tax on transfer of property in goods involved in the execution of works contract is paid on actual value, the same value is also taken for the purpose of determining the value of works contract service. In other cases, value of works contract service shall be determined based on the actuals. It has also been explained that value of works contract service shall include:

- (i) labour charges for execution of the works;
- (ii) amount paid to a sub-contractor for labour and services;
- (iii) charges for planning, designing and architect's fees;
- (iv) charges for obtaining on hire or otherwise, machinery and tools used for the execution of the works contract;
- (v) cost of consumables such as water, electricity, fuel, used in the execution of the works contract, the property in which is not transferred in the course of execution of a works contract;
- (vi) cost of establishment of the contractor relating to supply of labour and services;
- (vii) other similar expenses relating to supply of labour and services; and
- (viii) profit earned by the service provider relating to supply of labour and services;

9.4 If the gross amount charged for the works contract is inclusive of VAT or sales tax, the value for the purposes of service tax shall be computed as follows:

[Gross amount charged – (Value of transfer of property in goods involved in the execution of works contract and VAT or sales tax paid, if any, on the said transfer of property in goods involved in the execution of the said works contract)].

9.5 As a trade facilitation measure and also for ease of administrative convenience, the service provider has been given an option to adopt the composition scheme for payment of service tax on works contract service. The Works Contract (Composition Scheme for Payment of Service Tax) Rules, 2007 has accordingly been notified vide notification No.32/2007-Service Tax dated 22.05.07.

9.6 The scheme provides that the service provider shall have an option to pay an amount equivalent to two per cent. of the gross amount charged for the works contract instead of paying service tax at the rate specified in section 66. Gross amount charged for the works contract shall not include VAT or sales tax paid on transfer of property in goods involved in the execution of the said works contract. The provider of taxable service opting to pay service tax under the said composition scheme is not entitled to take CENVAT credit of duty on inputs, used in or in relation to the said works contract, under the provisions of CENVAT Credit Rules, 2004.

9.7 The provider of taxable service who opts to pay service tax under these rules shall exercise such option in respect of a works contract prior to payment of service tax in respect of the said works contract and the option so exercised shall be applicable for the entire works contract and cannot be withdrawn until the completion of the said works contract.

9.8 Presently, erection, commissioning or installation service [section 65(105)(zzd)], commercial or industrial construction service [section 65(105)(zzq)] and construction of complex service [section 65(105)(zzzh)] are separate taxable services.

9.9 Various trade and industry associations have raised apprehension in respect of classification of a contract either under the newly introduced works contract service or under erection, commissioning or installation and commercial or residential construction services.

9.10 Contracts which are treated as works contract for the purpose of levy of VAT / sales tax shall also be treated as works contract for the purpose of levy of service tax. This is clear from the definition under section 65(105)(zzza).

10. Changes explained above are not exhaustive and are only for the purpose of providing guidance. Explanations are not to be treated as part of the statutory provisions and do not override them. The statutory provisions and the relevant notifications have to be read carefully for interpreting the law. Any problems of implementation may kindly be brought to our notice.

With regards,

Yours sincerely,

(R. Sekar)  
Joint Secretary (TRU)

The Government has issued much awaited Notifications today bearing Notification No. 23-32/2007-ST, dated 22<sup>nd</sup> May 2007 giving effect to the amendment made through Finance Act, 2007 (detail notifications see <http://www.servicetax.gov.in> ). All the aforesaid Notifications shall come into force from 1<sup>st</sup> June 2007.

1. **Secondary and Higher Education cess:** The Government has levied 1% additional cess on the service tax payable on the taxable services. On the existing taxable services, such cess was

applicable from the date of enactment of Finance Act, 2007. Whereas, such cess on the new services as well as on the expansion of the existing services shall be applicable w.e.f. 1<sup>st</sup> June 2007.

There was lot of confusion about the date of applicability of this additional cess because the President had given the assent to Finance Bill on 11<sup>th</sup> May 2007, whereas, the Finance Act, 2007 was published in the Gazette of India on 12<sup>th</sup> May 2007. We have analysed this situation in the light of various Supreme Court decisions and we are of the view that it cannot be made applicable from the date of the assent of the President because a law shall be effective only from the date when it is notified or gazetted. Therefore, effective date for the applicability of this additional cess shall be 12<sup>th</sup> May 2007. Further, this is a separate cess has to be charged separately in the bill/invoice and separate record is required to be maintained. The assessee is required to deposit additional cess under a separate code which has been notified as "00440252" which needs to be enacted separately on the challan.

2. **Effective date of Service Tax for new Services:** The Government has notified 1<sup>st</sup> June 2007 as the date for applicability of service tax on the new services introduced by the Finance Act, 2007 vide Notification No. 23/2007-ST. The Government has introduced following 7 new services by the Finance Act, 2007 on which, now, service tax shall be applicable from 1<sup>st</sup> June 2007:

- a) Telecommunication service [section 65 (109a) read with section 65(105)(zzzx)]
- b) Mining service [Section 65(105)(zzzy)]
- c) Renting of immovable property service [Section 65(105)(zzzz) read with section 65(90a)]
- d) Service involved in the execution of a works contract [Section 65(105)(zzza)]
- e) Development and supply of content service [Section 65(105)(zzzzb) read with section 65(36c)]
- f) Asset management including portfolio management and all forms of fund management service [Section 65(105)(zzzzc)]
- g) Design services [Section 65(105)(zzzzd) read with section 65(36b)]

3. **Effective date of applicability of Service Tax on the expansion of existing Services:** By the Finance Act, 2007, the Government has expanded the scope of a number of existing services, service tax on such expansion of existing services shall also be applicable from 1<sup>st</sup> June 2007 vide Notification No. 23/2007-ST. The following existing services are amended by the Finance Act, 2007 to expand their scope:

- a) Sale of space or time for advertisement [Section 65(105)(zzzm)]
- b) Rent-a-cab service [Section 65(20)]
- c) Mandap keeper service [Section 65(66) and 65(67)]
- d) Pandal or shamiana service [Section 65(77a)]
- e) Event management service [Section 65(40)]
- f) Manpower recruitment or supply service [Section 65(105)(k)].
- g) Banking and other financial service [Section 65(105)(zm) read with Section 65(12)]
- h) Management consultant's service [Section 65(105)(r) read with Section 65(65)].
- i) Consulting engineer's service [Section 65(105)(g)]
- j) Management, maintenance or repair service [Section 65(64)]

4. **Service Tax on renting of Immovable Property for commercial purposes:** As expected, the Government has announced applicability of service tax on the rent of immovable property. However, the Government has given concession to the extent of property tax actually paid in respect of such properties. Therefore, service tax is liable to be paid on the rent received after deducting the property tax paid – vide Notification No. 24/2007-ST. In the said Notification, the provision has also been made for pro-rata benefit of property tax if the period for property tax and the rental period on which service tax is paid, do not match. However, the provision has also been made by amending the Service Tax Rules for making the provision of self-adjustment of excess service tax paid on account of non-availing of benefit of deduction of property tax, if the same has not been paid before the payment of service tax, however, such benefit can be taken within one year from the payment of property tax. In other words, where the assessee has not availed the benefit of concession of property tax then service tax so paid in excess can be adjusted subsequently vide Notification No. 28/2007-ST.

5. **Government has exempted the levy of Service Tax for Services involved in the execution of Works Contract in relation to construction of Port or other Port from the whole of Service Tax:** This exemption is similar to the exemption provided by Notification No. 16/2005-ST from the levy of service tax under the commercial or industrial construction service for

construction of Port which is now being omitted and replaced with Notification No. 25/2007-ST (vide Notification No. 25/2007-ST and 26/2007-ST).

6. **Service Tax on the Services involved in the execution of Works Contract:** The Government has conceded a long standing demand to improvise the levy of service tax in respect of Works Contract which was subject to State levy as well as Central levy and has the cascading effect. To remove this cascading effect, some provisions have been introduced so that both State and Central, levy should not be levied on more than the total transaction value. Whereas, earlier both State and Central (VAT and Service Tax) were charged on much more than the actual transaction value. However, this scheme had been launched only for the specified service namely, construction – both commercial and residential as well as turnkey project and benefit has not been extended to the rest types of Works Contract such as repair and maintenance.

a) **Composition Scheme:** The Government has introduced the Works Contract for Payment of Service Tax Rules, 2007 for providing easy mechanism to discharge the service tax liability in respect of the services covered under the category of Works Contract. Under these rules, which has the overriding effect over Section 67 and the Service Tax Valuation Rules, it has been provided that a person liable to pay service tax in relation to Works Contract services, has the option to pay service tax at an amount equal to 2% of the gross amount charged for the Works Contract, instead of paying service tax at the normal rate. Further, it has also been provided under the rule that the gross amount on which the service tax shall be payable under the Composition Scheme shall not include the VAT/ Sales Tax paid on the goods involved in the execution of Works Contract. Further, under the said rule, it has also been provided that those assessee who will opt for the Composition Scheme shall not be eligible to take the credit of excise duty and education cess paid on any input used in the execution of such Works Contract. Under the said rule, it has been further provided that assessee has to opt this option in respect of each Works Contract in the beginning itself and it cannot be changed (Vide Notification No. 32/2007-ST).

b) **Valuation of Services involved in the execution of Works Contract:** The Government has amended the Service Tax (Determination of Value) Rules, 2006 for determination of value of services involved in the execution of Works Contract by introducing rule 2A under the said rules. The service provider those who are not opting for the Composition Scheme and wish to pay the tax at the normal rate has the option to pay service tax at the normal rate on the value of service involved in the execution of Works Contract. The value of such services shall be determined in the manner prescribed in the said rules. As per the said rule, value of services involved in Works Contract shall be the gross amount charged for the Works Contract after deducting the value of the goods involved in the said Works Contract. However, VAT/ Sales Tax paid on such Works Contract shall not be included in the gross amount so charged. The said rule has further prescribed where the assessee has paid VAT/ Sales Tax on the value of the goods involved in such Works Contract, same value shall be taken as the value of goods for the determination of value of services by deducting from the gross amount charged for Works Contract (Vide Notification No. 29/2007-ST).



7. **Export of Service Tax and 'Import of Service Tax'**: The Government has made the consequential changes in the respective rule of export and import of services to incorporate the new services introduced by the Finance Act, 2007. However, the Government has also made a significant change in the Export of Services Rules, 2007 by which now it is mandatory for every taxable service, which is exported, receipt has to be only in convertible foreign exchange. Whereas, prior to the said amendment, the receipt in convertible foreign exchange was mandatory only for those services, which are provided outside India. In other words, the services which are provided in India but treated as export of services, there was no mandatory requirement that the receipt should be in convertible foreign exchange vide Notification No. 30-31/2007-ST.

***SERVICE TAX BOOKS AUTHORED BY J.K. MITTAL (UPDATED UP TO MAY, 2007) (to be released on 1<sup>st</sup> June 2007)***

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