

### DIGEST OF WORKS CONTRACT PROVISIONS UNDER VAT LAWS IN UTTARAKHAND

A works contract is a contract which involves labour as well as materials and where the materials are partially transferred. The quantum of materials could vary from contract to contract. The State law has the capability of only charging the tax on the goods and is not in a position to tax the service element of the transaction.

As a result of the 46th Amendment to the constitution, the contract which was single and indivisible was altered by a legal fiction into a contract which could be divisible into contract for sale of goods and contract for supply of labour and services. If the legal fiction introduced by Article 366(29A)(b) is carried to its logical end, it follows that even in a single and indivisible works contract there is a deemed sale of the goods which are involved in the execution of a works contract. After the 46th amendment, it has become possible for the States to levy sales tax on the value of goods involved in a works contract in the same way in which the sales tax was leviable on the price of goods and materials.

The difference between a sale and a works contract is that a sale involves transfer of property in the goods whereas in a works contract, there is only a contract to render work on the customer's property whether movable or immovable. Works Contract includes any agreement for carrying out for cash, deferred payment or other valuable consideration, the assembling, construction, building, altering, manufacturing, processing, fabrication, installation, fitting out, improvement, repair or commissioning of any moveable or immovable property. Transfer of goods involved in the execution of works contract is a deemed sale and therefore, works contract can be split into contract for labour and contract for sale. The transfer of property in goods involved in execution of works contract is chargeable to VAT. In arriving at the taxable turnover, various deductions from the contract receipts are allowed. The various deductions are in respect of labour charges, purchases of material from local registered dealers and payments to sub-contractors.

In the case of *Gannon Dunkerley and Co Vs. State of Rajasthan (SC) 88 STC 204*, the Hon'ble Supreme Court held that the measure of levy of the tax contemplated by Article 366(29-A)(b) is the value of goods involved in the execution of works contract. The value of goods for levying tax can be assessed only on the basis of cost of acquisition of the goods by the contractor and not on the basis of the value at the time of incorporation of such goods in the works contract as incorporation of the goods in the works forms part of the contract relating to work and labour which is distinct from the contract for transfer of property in goods. Therefore, the cost of incorporation of goods in the works cannot be made a part of the measure for levy of tax contemplated by Article 366(29A)(b).

Sale price in relation to transfer of property in goods whether as goods or in some other form is arrived at by deducting from the amount of valuable consideration paid or payable to a person for the execution of the works contract, the amount representing labour charges for such execution.

In *Gannon Drunkenly and company and others vs. State of Rajasthan and others (1993) 88 STC 204 (SC)*, it was stated that the value of the goods involved in the execution of works contract will have to be determined by taking into account the entire value of the contract and deducting there from the charges towards labour and other services. In other words labour, service and other charges not relating to transfer of property has to be deducted from the total consideration of works contract. Where such labour and other service charges are not quantifiable, the sale price shall be the cost of acquisition of the goods and the margin of profit on them prevalent in the trade plus the cost of transferring the property in the goods and all other expenses in relation thereto till the property in them, whether as such or in any other form, passes to the Contractee and where the property

passes in a different form shall include the cost of conversion. The value of the goods involved in the execution of a works contract will, therefore, have to be determined by taking into account the value of the entire works contract and deducting there from the charges towards labour and services which would cover :

- (i) labour charges for execution of works
- (ii) amount paid to sub-contractor for labour and service
- (iii) charges for obtaining on hire or otherwise machinery and tool used for execution of the works contract
- (iv) charges for planning, designing and architect's fees
- (v) cost of consumables used in the execution of the works contract
- (vi) cost of establishment of the contractor to the extent it is relatable to supply of labour and services
- (vii) other similar expenses relatable to supply of labour and services and
- (viii) profit earned by the contractor to the extent it is relatable to supply of labour and services.

The transfer of property in goods (whether as goods or in some other form) involved in the execution of works contract is sale of the goods. Under the VAT System, tax is to be charged on each sale of taxable goods and tax invoice showing the tax element separately is to be issued in respect of every sale of taxable goods in the State by a registered dealer.

If a *contractor-registered dealer* is engaged in the execution of works contract of moveable property of a Contractee in the State and is not availing the composition scheme of paying a lump-sum amount in lieu of tax, then he will charge tax on the value of goods transferred in the works contract and will issue tax invoice to the Contractee. In case the Contractee is a registered dealer under the Act, he would claim input tax credit in respect of such goods received in the works contract from the contractor. The contractor-registered dealer will also be entitled to claim input tax credit in respect of the goods purchased from within the State, which were transferred in the execution of the works contract.

If a *contractor-registered dealer* is engaged in the execution of works contract of immovable property of a Contractee in the State and is not availing the composition scheme of paying a lump-sum amount in lieu of tax, then he will charge tax on the value of goods transferred in the works contract and will issue tax invoice to the Contractee. The Contractee would not be entitled to claim input tax credit in respect of the goods received in the works contract. However, the contractor registered dealer will be entitled to claim input tax credit in respect of the goods purchased in the State, which were transferred in the execution of the works contract.

If a *contractor-registered dealer* is availing composition scheme as applicable under the relevant State VAT Act and is engaged in the execution of works contract of immovable property of a Contractee in the State, then he is not entitled to charge tax in respect of the goods transferred in the works contract.

The contractor registered dealer is also not entitled to claim input tax credit in respect of purchase of any goods from within the State, which were transferred in the execution of works contract of the immovable property to the Contractee. The Contractee registered dealer will also be not entitled to claim input tax credit in respect of the goods received by way of transfer in the works contract of immovable property from the contractor -registered dealer.

If a *contractor-registered dealer* is availing composition scheme as applicable under the relevant State VAT Act and is engaged in the execution of works contract of moveable property of a

Contractee in the State, then he is not entitled to charge tax in respect of the goods transferred in the works contract and will not issue tax invoice to the Contractee. The contractor- registered dealer is also not entitled to claim input tax credit in respect of purchase of any goods from within the State, which were transferred in the execution of the works contract. The Contractee- registered dealer will also be not entitled to claim input tax credit in respect of the goods received by way of transfer in the works contract of moveable property, from the contractor registered dealer.

The rates of tax applicable to various kinds of works contract are specified in respective schedules. The transaction can be considered to be works contract generally only if there is any accession or accretion to the property of the customer. Purely labour contracts not involving supply of any goods by the contractor to his customer will not attract any VAT or works contract tax.

As a basic feature, tax is chargeable on the transfer of property in goods involved in the execution of works contract at the rates prescribed for the concerned goods in the schedules of the concerned State VAT legislation. Where value of each item of material transferred in the course of execution of works contract is identifiable, tax can be charged on the value of individual items of materials as provided under the schedules to the concerned State VAT Legislation. On inputs, the contractor is entitled to avail Input Tax Credit (ITC).

Most of the State VAT laws provide input tax credit on inputs used for executing Works Contract. Some States however, are not considering consumables at par with inputs. In case of composition schemes some States do not allow any input tax credit while in some States allow partial tax credit.

The following are certain important principles with respect to works contracts:

- There should be transfer of property in goods.
- Pure labour contracts or service contracts are outside the purview of the works contract under the State law. In case if any of the goods are consumed during the execution of works contract and their identity is lost and accordingly there is no transfer of property in goods then in such instance such consumables are not leviable to VAT under the State VAT law.
- There must exist an individual and composite works contract. The divisible contracts are outside the scope of the works contract.
- Transfer of property in goods must pass as goods or in some other form. Form of goods has no relevance.
- In works contract transaction vesting of property must occur not by contract but on the theory of accretion and accession.
- There must be dominant intention to affect the transfer of property in goods in execution of works contract, passing of the property in goods must not be only incidental to the contract.
- Such transfer of property in goods may be in the form of goods itself or in some other form.
- Such goods, which are being transferred, should be involved in the execution of works contract.

If any of the above said propositions are not fulfilled, then the activity is not covered under the scope of levy under VAT. However, there are numerous decisions in this context under various sales tax laws considering different types of activities independently. Therefore, though the above is only a broad principle, each transaction would be required to be examined in the light of the circumstances and the decided case laws as may be applicable to the goods dealt in with by them. Considering the above factors, it becomes essential to identify whether the activity is covered under the scope of levy in the course of execution of works contract or not. If it is so covered, then the next question would be the quantification of such levy. The quantification of tax levy will be based on the tax rate, which has to be applied on the value to be determined.

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<b>S No.</b>	<b>Particulars</b>	<b>Yes/No</b>	<b>Relevant Section/ Rule</b>
1	Is works contract dealt separately under the VAT Act?  Is there a deeming provision dealing with works contract?	Yes	Section 2(55) of the Uttarakhand Value Added Tax Act, 2005 (the VAT Act)
2	Is there any specific form to apply for registration as a works contractor (WC) under VAT law?	No	Section 15 of the VAT Act Rule 14 of the Uttarakhand Value Added Tax Rules,
3	Whether Non- resident (dealer outside the state) can apply for registration towards works contract?	Non- resident (dealer outside the state) cannot apply for registration towards works contract.	
4	Eligible Turnover for registration.	Eligible turnover for registration is 5 lacs.	
5	What are the deductions that are allowable from turnover?	The following amounts shall be deducted from the turnover of the works contractor :- (a) Sale value of the goods covered by section 3, section 4 and section 5 of the CST Act, 1956; (b) The value of goods exempted under any provision of the Act; (c) The value of goods on the sale of purchase where tax has been levied or leviable under the Act at some earlier stage; (d) The value of goods supplied to the contractor by the contractee, but the ownership of such goods remains with the contractee; (e) The amount representing labour charges for the execution of works contract; (f) The amount paid to	Rule14(2) of the VAT Rules.

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		sub-contractors as the consideration of execution of works contract; (g) The amount representing the charges for planning, designing, and architects fees; (h) The amount representing the charges for obtaining on hire or otherwise machinery and tools; (i) The amount representing the cost of consumables.	
6	Whether the WC has the option to claim the labour charges and like on actual basis or adhoc basis?	Actual basis	Rule 14(2) of the VAT Rules.
7	How are the labour charges and like defined under the VAT law?	Labour and like charges includes: (a) Labour charges for execution of the works; (b) Charges for planning, designing and architect fees; (c) Charges for obtaining on hire or otherwise machinery and tools used for the execution of the works contract; (d) Cost of consumables such as water, electricity, fuel, etc., used in the execution of the works contract, the property in which is not transferred in the course of execution of a works contract; (e) Cost establishment of the contractor to the extent it is relatable to supply of labour and services; (f) Other similar expenses	Rule 14(2) of the VAT Rules.

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		relatable to supply of labour and services; (g) Profit earned by the contractor to the extent it is relatable to supply of labour and services.	
8	Whether depreciation can be claimed as labour charges and like? If yes, then whether input tax credit on capital goods will be allowable?	No, Depreciation cannot be claimed as labour and like charges.	Rule 14(2) of the VAT Rules.
9	Can deduction be claimed for land value by the composition dealer?	No specific provision allowing the Same	
10	How is the estimated gross profit computed in case of work contract?  Also, what is the ratio to apportion the gross profit between material and labour?	No specific provision  No specific provision	
11	Whether gross profits are to be added to actual labour charges and like or adhoc labour charges and like?	Gross profit is to be added to actual labour and like charges.	Rule 14(2) of the VAT Rules.
12	Whether water, electricity deposits, stamp duty, registration fee, service tax, etc form part of the works contract turnover?	No, these contracts does form a part of the works contractor turnover.	Rule 14 of the VAT Rules.
13	Is contractor liable to tax for free supply of goods by contractee?	The value of goods is allowed as deduction from taxable turnover	Rule 14(2) of the VAT Rules.
14	What is the time of sale for works contractor and at what point of time the tax should be offered to the department?	Generally, at the time goods are incorporated in work.	
15	Which Section /Schedule prescribes the rate of tax for works contract?	Section 3 is applicable to know the rate of tax for works contract.	Section 3 of the VAT Act.
16	Whether WC will be liable to pay unregistered purchase tax in addition to works contract tax?	No separate provision. However, certain specified purchases are eligible to VAT in the state.	
17	What is the rate of tax for declared goods used in the course of contract?	No specific provision	
18	Is standard deduction method available for payment?  If yes, what are the various rates	No separate rates for different types of works contract	

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	prescribed for different types of works contract?		
19	Whether contractee / principal is liable to deduct TDS from the amount payable to contractor?	Yes, Contractee/Principal is liable to deduct the TDS from the amount payable to contractor.	Section 35 of the VAT Act.
20	What is the rate of TDS to be deducted in case of works contract?  Whether interstate supplies or import transactions are considered for deducting TDS?	Rate of TDS Deduction is 4%.  No	Rule 21 of the VAT Rules.  Section 35 of the VAT Act.
21	Is the contractor also liable to deduct TDS from the amount payable to the Sub-Contractor?	Yes, the contractor is liable to deduct TDS from the amount payable to the sub-contractor.	
22	Whether the WC can claim input tax credit on consumables?	Input tax credit is allowed on consumables as consumables are excluded from the value of net turnover for the purpose of works contract.	Section 6 of the VAT Act read with Rule 14 of the VAT Rules.
23	Whether deduction for sub contractor turnover is permitted from the turnover of WC?  Does WC have the option to claim input tax credit in lieu of deduction from total turnover?	Yes  When such turnover does not form part of taxable turnover, credit of such turnover shall not be allowed.	Rule 14(2) of the VAT Rules.
24	Whether input tax credit is allowable fully in case of works contract?	No	Section 4 and 6 of the VAT Act.
25	Is there any specific format of invoice or bill for regular and composition WC?	No	
26	Can Running bill be treated as Invoice? Whether advances received including mobilization advance will be liable to tax?	Yes  No specific provision for advances.	
27	Is it compulsory for the subcontractor to be a registered dealer and file returns declaring the turnover	Yes For the purpose of claiming deduction, the sub-contractor should be a registered dealer and	Rule 14(2) of the VAT Rules.

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		should have filed the return declaring the turnover pertaining to main contractor.	
28	Can sub-contractor claim exemption if main contractor pays tax?	Yes	Section 7 of the VAT Act.
29	Whether contractor or subcontractor are exempted in case any one of the two undertakes to discharge VAT liability on the entire consideration?	No, there is no such option Available.	
30	Does the WC have an option to pay tax under composition category?	Yes WC have an option to pay tax under Composition Category	Section 7 of the VAT Act.
31	Is composition WC allowed to make interstate / import purchases?	Yes Registered dealers engaged exclusively in works contracts in the nature of civil construction or electrical work and procuring goods with their worth exceeding 5% from outside Uttarakhand [composition scheme (01.04.2012 to 31.03.2015)]	
32	Is composition WC eligible to take sub-contractor deductions?	Yes, composition WC dealer is eligible to take sub-contractor deductions.	Rule 14(2) of the VAT Rules.
33	Whether WC can opt for regular scheme for one project and composition scheme for other project?	No	
34	Is there any procedure to change the scheme from regular to composition works contractor?	There is no such procedure specified in the act.	
35	Is there any procedure to change the scheme from composition to regular works contractor?	There is no such procedure specified in the act.	
36	What are the composition rates for different types of contracts?	N.A.	
37	Whether WC opting for composition method is required to take prior permission/ provide intimation to the department?	No, it is not required to provide intimation to department.	
38	Whether composition dealer can	No, he cannot apply for	

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	apply for interstate works contract?	interstate works contract.	
39	Whether such WC is required to file monthly / quarterly return? What is the due date of filing the return?.	Quarterly return  25th of the first month of the next quarter.	Rule 11 of the VAT Rules.
40	Whether Annual Return is filed by the works contractor?	Yes, the work contractor has to file an Annual return in Form IV(B)	Rule 11 of the VAT Rules.
41	What is the time limit for Assessment in case of works contractor?	No time limit specified.	
42	Whether VAT Audit provisions, if applicable under the State VAT law, apply to WC as well?  If yes, what is the turnover limit for such audit?	Yes VAT Audit Provisions applies to WC also. If total turnover in a year exceeds 40 Lacs Accounts shall be audited annually by a Chartered Accountant or Cost Accountant or person specified in Section 226(2) of Companies Act, 1956 and copy of audited statement of accounts and report shall be obtained before 31st October and furnished within 2 months from end of 31st October	Section 62 of the VAT Act.
43	Whether VAT is applicable on sale of flats by the developer pertaining to the share of developed area in case of construction contracts?	No specific provision	
44	Is there a requirement to file the copy of contract / agreements with the department?	There is no such requirement.	