

Article on Reverse Charge

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Introduction

Reverse charge is a not nearly as new as our recollection of service tax being required from the service recipient. Reverse charge is how customs duties are collected. Reverse charge is how excise duty was collected in case of molasses in some instances. GST only makes good use of this form on administering tax. It can't be said better than the words of Sir Maurice Gwyer in re the Central Provinces and Berar Act XIV of 1938 the learned JJ said *"Subject always to the legislative competence of the taxing authority, a duty on home-produced goods will obviously be imposed at the stage which the authority find to be the most convenient and the most lucrative, wherever it may be; but that is a matter of the machinery of collection, and does not affect the essential nature of the tax"*

GST that is levied on the subject of taxation is generally payable by the supplier but in specified cases, the recipient is required to discharge the liability.

Specific Reverse Charge

Reverse charge is provided in the case of intra-State supplies listed vide notification 4/2017-Central Tax (Rate) dated 28 June, 2017 with respect to supply of goods and 13/2017-Central Tax (Rate) dated 28 June, 2017 ('the notification') with respect to supply of services.

GST defines 'reverse charge' very plainly that the 'recipient of supply' is liable to pay tax in cases specifically provided by section 9(3) and in other cases provided by section 9(4) of the CGST Act. It is interesting to see that there are two separate provisions to recover GST from the recipient. Reverse charge is defined as:

2(98) "reverse charge" means the liability to pay tax by the recipient of supply of goods or services or both instead of the supplier of such goods or services or both under sub-section (3) or sub-section (4) of section 9, or under sub-section (3) or subsection (4) of section 5 of the Integrated Goods and Services Tax Act

First Step

In order to attract collection of tax from the recipient, the levy of tax on the supply must first be established.

Supply	Ingredients for Supply		
section 7(1)(a)	All forms of supply	For consideration	In business
section 7(1)(b)	Import of services	For consideration	NA
section 7(1)(c)	Specified in sch I	NA	In business
section 7(1)(d)	Specified in sch II	NA	Only if required in an entry

So, it is very important that this ‘first step’ must be taken relating to levy of GST before proceeding to recover this levy from the recipient. Recovery of tax from the recipient is provided as follows:

9. (1) Subject to the provisions of sub-section (2), there shall be levied a tax called the central goods and services tax on all intra-State supplies of goods or services or both, except on the supply of alcoholic liquor for human consumption, on the value determined under section 15 and at such rates, not exceeding twenty per cent., as may be notified by the Government on the recommendations of the Council and collected in such manner as may be prescribed and shall be paid by the taxable person.

(2)

(3) The Government may, on the recommendations of the Council, by notification, specify categories of supply of goods or services or both, the tax on which shall be paid on reverse charge basis by the recipient of such goods or services or both and all the provisions of this Act shall apply to such recipient as if he is the person liable for paying the tax in relation to the supply of such goods or services or both.

That the supplier – taxable person – who is liable to pay has now passed on to the recipient to pay. Every recipient is required to identify under which limb of section 7(1) does the levy stand attracted. In other words, it is possible that a transaction resembling a supply may not actually be liable because it missed the ingredients of all four limbs of section 7(1) such that this ‘first step’ never existed for the rest of the law to apply.

Second Step

After the levy has attracted, the next step would be to identify the recipient in order to fasten this liability. Recipient is defined as:

2(93) “recipient” of supply of goods or services or both, means—

(a) where a consideration is payable for the supply of goods or services or both, the person who is liable to pay that consideration;

(b) where no consideration is payable for the supply of goods, the person to whom the goods are delivered or made available, or to whom possession or use of the goods is given or made available; and

(c) where no consideration is payable for the supply of a service, the person to whom the service is rendered,

and any reference to a person to whom a supply is made shall be construed as a reference to the

recipient of the supply and shall include an agent acting as such on behalf of the recipient in relation to the goods or services or both supplied;

So, it is an important 'second step' to correctly identify the person who is required to discharge the liability. Please note that GST introduces us to the concept of 'distinct person' which subdivides the person into multiple distinct persons. And the responsibility to pay the tax resides not on the person but on the distinct person concerned. It is not uncommon for payments to be centralized in large corporations. In such cases, the manner of reporting compliance must demonstrate to have been discharged by the distinct person concerned.

Third Step

Once the liability to pay GST is placed on the shoulders of the recipient, then it must be recognized that that liability never resided on the shoulders of the supplier. The 'third step' is to exonerate the supplier from this liability. What this means is that this path of reverse charge is a 'without recourse' path. In the event of default by the recipient, the liability does not get restored on to the supplier. Once the supply is notified by the Government under section 9(3), then the liability to pay permanently resides on the recipient including consequences and remedies. And the supplier is immune from the levy. Support to this interpretation from the words 'as if' used in the section.

'As if' demands that a certain state of fiction be visualized and the administration follow this path of fiction 'as if' it were the reality. When a fiction is required to be considered 'to be' the reality, then the 'reality' is required to be displaced and dispatched out of consideration.

There is no recourse back to the supplier in any circumstance.

Third Step Modified

Now, the notification identifies the supply in column (4) the person liable to pay tax is identified in column (5) in the case of goods (and in the case of services, column (3) and column (4) respectively). Interestingly, there seems to be some filtration that is built in the notification because it does not stop at saying 'recipient' but uses expressions like 'business entity' (in sl. no. 2) or 'company or body corporate' (in sl. no. 6) of notification for services. As a result, it is not that all supplies listed in the notification require payment of tax by the recipient but only a sub-set of cases, that is, where the supply is notified and the recipient is of the kind specified in the same notification will the liability now reside on the said recipient.

Though a supply may be specified in the notification, but if the recipient does not fit the description in the notification, then the third step stands 'reversed'. That is, the liability to pay tax reverts back to the supplier.

Please note that the liability to pay tax always resides on the taxable person who is the supplier:

2(107) "taxable person" means a person who is registered or liable to be registered under section 22 or section 24

2(105) "supplier" in relation to any goods or services or both, shall mean the person supplying the said goods or services or both and shall include an agent acting as such on behalf of such supplier in relation to the goods or services or both supplied

But, where the mechanism of reverse charge is put into operation, then the supplier will be supplemented with the recipient for discharging the liability to deposit tax levied. Care should be taken to identify if the recipient fits the description of description in the notification. For example, tax on GTA services provided to a non-corporate will have to be discharged by the GTA and not the recipient and all conditions attached in the notification prescribing the rate of tax will apply to the GTA while paying the tax.

General Reverse Charge

While section 9(3) applies only to those supplies listed in the notification, there is yet another provision which borrows the mechanism of reverse charge in section 9(4) and mkwhich states as:

(4) The central tax in respect of the supply of taxable goods or services or both by a supplier, who is not registered, to a registered person shall be paid by such person on reverse charge basis as the recipient and all the provisions of this Act shall apply to such recipient as if he is the person liable for paying the tax in relation to the supply of such goods or services or both.

The implication is that in every instance where the supplier is unregistered, the 'registered recipient' will be liable to pay tax. So, the three-step process that was identified earlier stands modified somewhat.

- First Step – same
- Second Step – no requirement for notification but, the recipient must be 'registered'
- Third Step – same

Here, it does not matter 'why' the supplier is unregistered – he may enjoy threshold benefit or may be avoiding registration or may be excluded from registration by section 23 – whatever is the reason, the fact that 'supplier is unregistered' is sufficient to place the burden on the recipient. Please note that this provision will fail to operate if both supplier and recipient are unregistered. This provision will apply only if the recipient is registered and the supplier is unregistered. For example, if an advocate who is not liable to be registered engages a supplier of paper who is unregistered, this provision will not operate.

Please note that it is not required that the supplier must charge GST on his supplies. The requirement is merely for the supplier to be unregistered. A supplier who has opted for

composition would not charge GST on his supply but is nevertheless registered and does not attract this provision. Registered persons are welcome to receive supplies from composition tax payers and not be anxious about section 9(4).

Apart from the above, the apprehension is that every registered person needs to look out for inward supplies from unregistered persons. One might go to the extent of stating that 'every debit' in the books of a registered person must appear on GSTR-1 of one or other supplier. And if it does not, then such inward supplies must be treated through the registered persons' GSTR-2. This is an interesting general rule but has exceptions, namely:

- Supply must be a taxable *qua* the unregistered supplier – this is a case where the inward supply (so called for ease of reference) is not a 'taxable supply' in the hands of the person supplying (who is found to be unregistered). For example, press release (unnumbered) dated 13 July, 2017 states that gold ornaments 'traded in' by a consumer (sold to jeweler) does not attract section 9(4) in the hands of the registered jeweler for the reason that this is not a 'taxable supply'. This conclusion comes from a careful application of the 'first step' stated above. But, the question that arises is, can the registered person (jeweller) assume authority to reach into the affairs of the consumer (who brings the old ornaments) to examine and reach a correct conclusion on this fundamental question of fact – Is it taxable under one of the limbs of section 7(1)? Surely, the press release cannot grant *carte blanche* exclusion to jewellers or sanctioned such powers even though the apparent facts may lead (at best) to a suspicion that it may not be taxable. And how does the jeweler defend the exercise of this judgement in each case. Only time will tell but the press release has not only brought glee to this trade but all others who appear to have extended it to their own facts by analogy
- Supplies that are excluded by sch III such as payments to employees and duly subjected to income-tax as salary. Here too, another press release (unnumbered) and dated 10 July 2017 has been issued offering clarity and causing some ambiguity that perquisites that are subject to income-tax are excluded from GST if they comprise of contractual obligations of employer to pay the employee. Surely, this does not put to rest all concerns. The concerns that remain are policy-driven payouts that are not subjected to income-tax. While this press release may be attractive to shove 'all payments by employer to employee' as excluded from GST, the unintended by product would be that such an interpretation affords opportunity to 'pass through' employee all inward supplies from unregistered suppliers. The last word has not yet been spoken on this one but meticulous application of the above principle is key and a cautious person would claim available credit and pay output tax rather than forego credit bravely resisting tax on these "not-within-salary" payments.
- Expenses accounting towards depreciation and amortization as they do not represent supply much less taxable supply

- Supplies such as interest on loans and other inward supplies that are specifically exempted

Lateral Charge on Ecommerce

All though the above two cases are listed in section 2(98) as 'reverse charge', there is another provision which deserves mention in the context of reverse charge. And that provision is the liability of ecommerce operator to pay tax on supply of services through the digital platform or network and for this reason, it can be referred as *Lateral Charge* as it is neither a forward or reverse charge. This is provided in section 9(5) of the CGST Act, which states:

(5) The Government may, on the recommendations of the Council, by notification, specify categories of services the tax on intra-State supplies of which shall be paid by the electronic commerce operator if such services are supplied through it, and all the provisions of this Act shall apply to such electronic commerce operator as if he is the supplier liable for paying the tax in relation to the supply of such services: Provided that where an electronic commerce operator does not have a physical presence in the taxable territory, any person representing such electronic commerce operator for any purpose in the taxable territory shall be liable to pay tax: Provided further that where an electronic commerce operator does not have a physical presence in the taxable territory and also he does not have a representative in the said territory, such electronic commerce operator shall appoint a person in the taxable territory for the purpose of paying tax and such person shall be liable to pay tax.

The reasons why this provision deserves special mention are:

- It is excluded from the definition of 'reverse charge' yet tax is not payable by the supplier
- It is tax payable by a person who is not the recipient but a third person facilitating supply
- It is tax payable not as if the 'person liable' to pay tax but as if the 'supplier liable' to pay tax

Notification 17/2017-Central Tax (Rate) dated 28 June, 2017 specifies that 'ecommerce operator' is liable to pay tax 'as if he is the supplier liable to pay tax' and lists the following:

- (i) services by way of transportation of passengers by a radio-taxi, motorcab, maxicab and motor cycle;*
- (ii) services by way of providing accommodation in hotels, inns, guest houses, clubs, campsites or other commercial places meant for residential or lodging purposes, except where the person supplying such service through electronic commerce operator is liable for registration under sub-section (1) of section 22 of the said Central Goods and Services Tax Act.*

The effect of this language deserves special mention of the following effects that are a departure from section 9(4) to the extent that:

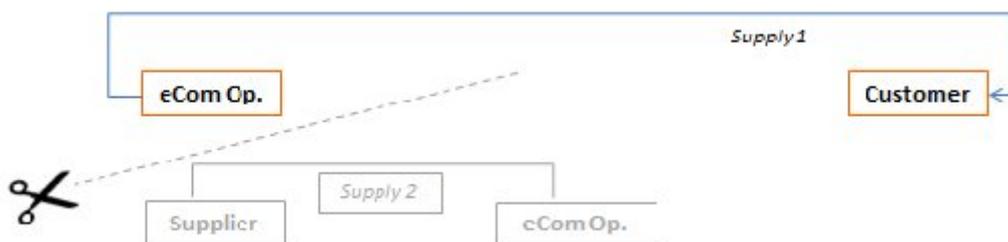
- Not only is the actual supplier not liable to tax (substitutionary effect)
- But also that the supply of services by the ecommerce operator to the actual supplier gets subsumed

Substitutionary effect has been explained earlier in the context of section 9(4) but this 'subsuming effect' may be discussed now. There are two supplies involved here, namely:

- Service provided by the actual supplier (taxi driver) to the passenger – taxi service
- Service provided by the ecommerce operator to the actual supplier – commission for securing customer for taxi service



Now, the language of section 9(5) produces the following effect:



Ecommerce operator having been treated as the ‘supplier liable to tax’ in ‘Supply 1’, he cannot at the same time continue to be treated as a commission agent in ‘Supply 2’. The fiction created must be carried through to its ‘purposeful end’ in this provision, that is, Supply 2 would be subsumed into Supply 1. There is no further tax payable on Supply 2 when the entire tax on Supply 1 at the full value is paid by the ecom operator.

Further, on looking into section 24, we find that the actual supplier where section 9(5) applies, is excluded from compulsory registration. In fact, when the tax liability is fastened on the ecom operator, the actual supplier is excluded from registration even if he crosses threshold benefit since section 24 overrides section 22 provided the actual supplier has no other taxable supplies.

IGST-CGST-SGST

The entire discussion above has been based on ‘intra-State’ supplies. With identical provisions appearing in section 5(3), (4) and (5) of IGST Act, the above discussion will apply even in case of ‘inter-State’ supply. In case of tax payable by ecom operator, notification 14/2017-Integrated Tax (Rate) dated 28 June, 2017 applies the tax on inter-State supplies.

Only one aspect to mention here is that when a transaction is an inter-State supply and liable to payment of IGST but not paid, then section 5(4) is attracted. However, if the ‘place of supply’ and ‘location of (unregistered) supplier’ are in the same State, then even though no tax has been paid, section 5(4) cannot apply. The reason being tax that should have been paid is CGST-

