

Issues on Job Work provisions under GST from perspective of manufacturers – mainly the Engineering and Automobile sectors

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Focus:

In this article, we have focussed on the issues on Job Work provisions under GST from perspective of manufacturers – mainly the Engineering and Automobile sectors who currently operate extensively under job work arrangements as envisaged under Central Excise. It may be noted that the procedure of paying the GST on supply (removal) to the job worker and job worker sending back with GST on the entire value including his value addition is also an option which is available in old law as well under GST.

Preliminary:

Job –work sector constitutes a significant industry in Indian economy. Its outsourced activity of working on the goods belonging to manufacturer. The parties undertaking operations on job work are by and large small parties, who would find it difficult to comply the detailed provisions of taxation.

Job Work is now a well settled procedure under the Central Excise whereby a manufacturer can send out inputs – either raw material or semi-finished material or the capital goods to another party - job worker - for further processing, testing, repair, reconditioning or for the manufacture of intermediate goods necessary for manufacture of final products or for any other purpose and receive back after processing the inputs or the products produced therefrom or the capital goods for use in further manufacture, without the manufacturer or the job worker having to pay any duty on the inputs or capital goods so sent out. This is subject to following the prescribed conditions and restrictions. The charges paid to the job worker, in common parlance referred to as labour charges, are also exempt from Service Tax provided the goods are subject to excise duty, a condition which is generally met. Under the state VAT Laws, there are no specific provisions dealing with job work procedure but the labour charges are exempt from payment of VAT. Job work process is very widely used in manufacturing industries and a number of operations such as cleaning, shot blasting, deburring, cutting, pressing, repair, machining, assembly/manufacture of intermediate goods etc. as are done under the job work process. The job work being a beneficial provision, the concept, though with some modifications, is continued under GST.

The advantage of job work procedure is that the goods can be sent out for further processing and received back without payment of tax at either end with the responsibility of what the job worker does resting with the manufacturer who sends the goods out for processing. This

relieves the job workers of the onerous responsibility of availing input tax credit and paying output tax. **The job work related provisions under the GST are briefly given below, sometimes comparing them with provisions under Central Excise from where these provisions under GST originate:**

1. Section 2(68) of the CGST Act – ‘job work’ means **any treatment or process** undertaken by a person **on goods belonging to another registered person** (referred to as Principal) and the expression ‘job worker’ shall be construed accordingly. Since the words used are ‘any treatment or process’, the scope of the term job work is very wide. While the person sending the goods out for job work (i.e. Principal), has to be a registered person, the job worker may or may not be a registered person though operationally it would be advisable to deal with a registered person only as job worker.

2. Schedule II of the CGST Act– any treatment or process which is applied to another person’s goods is a supply of services. Thus, the charges for the job work done, in common parlance, labour charges, will attract GST (in the absence of any exemption as under the current service tax law) as supply of service @18%. However, since input tax credit would be available for the same, this would not add to cost.

3. Sections 19 and 143 of the CGST Act - Principal can send inputs (or capital goods) outside for job work under intimation taking input tax credit thereon, and without disturbing the credit or without payment of tax and from there he can subsequently send them to another job worker and likewise. He can bring back within the specified time the inputs, after completion of job work or otherwise (or capital goods) to any of his place of business also without payment of tax. The Principal shall be entitled to take credit of input tax on inputs (or capital goods) even if inputs (or capital goods) are directly sent to job worker for job work without being first brought to his place of business.

4. Explanation to Section 143 of the CGST Act – for the purpose of job work, input includes intermediate goods arising from any treatment or process carried out on the inputs by the principal or the job worker. Thus, the inputs after they have undergone some process at the end of principal or job worker can be sent on job work for further treatment or process.

5. Section 143 of the CGST Act - the principal is accountable for the inputs (or capital goods) sent on job work. In particular, he has to ensure that they are brought back, within specified period of one year or three years respectively of the inputs or capital goods being sent out, after completing job work or otherwise, to any of his place of business. Alternately, he can declare the place of business of job worker as his additional place of business (or where the job worker is a registered under Section 25), and supply the inputs (or capital goods), after completing the job work or otherwise, from place of business of the job worker on payment of tax or export them under bond from such place which again has to be done within the aforesaid specified period of one year or three years respectively.

6. Failure to comply will result into liability on the Principal to treat the inputs (or capital goods) to the extent not brought back or supplied from job worker’s business premises, as supplied to the job worker on the day they were sent out to job worker and accordingly pay tax and interest. Moreover, since there is no provision for relaxation of time frame of one year & three years respectively for input and capital goods to be brought back or supplied from job worker premises and as the input tax credit for the tax so paid may not be available to anyone,

in order to avoid such cost, it is utmost essential that inputs (or capital goods) are brought back or supplied within the time frame and proper record of movement maintained. With regard to time frame for bringing back the inputs or capital goods, only exception provided is for jigs, moulds, dies, fixtures and tools which generally once sent to a particular job worker, remain with him for a long time often till their useful life. (Section 143 of the CGST Act).

7. The above provisions are on the lines of current provisions of Rule 4 (5) of CENVAT Credit Rules except that under the CENVAT Credit Rules, there is no requirement of intimation but these provisions under GST are more liberal in so far as supplies from job worker's premises are concerned since under the CENVAT Credit Rules, such arrangement is subject to order under Rule 4(6) from jurisdictional Deputy / Assistant Commissioner granting permission on the conditions he may impose to protect revenue. Moreover, while the time frame under the GST provisions to get back the inputs (or capital goods) after job work is longer, it is rigid and if not met, the tax amount may be lost with interest as against the provision under the CENVAT Credit Rules which allows availing credit again where the inputs or capital goods are received back after the stipulated period.

8. As per Input Tax Credit & Invoice Rules under GST, the inputs, semi-finished goods or capital goods are required to be sent by the principal to the job worker under the cover of a delivery challan containing specified details including where the goods are sent directly to job worker. The details of challans in respect of goods dispatched to a job worker or received from a job worker during a tax period are required to be included in Form GSTR 1 (outward supplies) for that tax period. Where the inputs or capital goods are not returned to the Principal within the time stipulated under Section 143, the delivery challan shall be deemed to be invoice for the purposes of GST provisions.

9. As per Section 143 of the CGST Act, there is no requirement that scrap generated at job worker end has to be brought back by the Principal. It may be supplied by the job worker directly from his place of business on payment of tax, if such job worker is registered, or by the principal if the job worker is not registered. Since the Principal is responsible for proper accounting it is nevertheless advisable that he ensures that scrap is properly disposed of paying tax thereon. Another related issue is that the job worker is often allowed to retain the scrap and its value is adjusted in arriving at labour charges. In that case, considering the provisions of Valuation Rules, scrap value will have to be added to labour charges for payment of GST thereon by the job worker.

10. As per transition provisions, where inputs as such or partly processed inputs are sent to job worker prior to appointed day under provisions of Central Excise, and if such goods are returned within six months of the appointed day, no tax would be payable. However, if such goods are not returned within the prescribed time, the input tax credit availed on such goods will be liable to be recovered from manufacturer. The manufacturer and the job worker are required to declare the details of such goods sent / received on job work and held in stock on the appointed day in prescribed format GST TRAN 1 within 90 days of the appointed day. It is imperative that the manufacturer and job worker properly reconcile their records in advance and the details provided by them in respective GST TRAN 1 match.

As mentioned earlier, the definition under GST of the term job work is quite wide. Under GST, the arrangement can be continued to be used for outsourcing number of manufacturing processes as currently done under Central Excise. This can be done without affecting the input tax credit or without paying tax while sending inputs (or capital goods) out on job work or while receiving the same back by following the procedure, which is substantially on the lines of CENVAT Credit Rules, subject to change that labour charges will attract GST and keeping in mind the rigidity of provisions on time frame. Similarly, the facility for sending dies, moulds, fixtures etc. as required at job worker end without disturbing the credit thereon continues as under Central Excise. Hence, the job work procedure will continue to be extensively followed by manufacturers in Engineering and Automobile sectors. At the same time, the benefit in sales tax currently there in the job work will be neutralized in GST and the decision (particularly true for large organizations) on whether to go in for job work or ask the supplier to procure all the material, will substantially depend on operational & pricing considerations.

Few specific issues concerning job work are dealt with in subsequent paras.

A. Job Work arrangement with related person – will goods sent to job worker who is a related person be treated as supply under provisions of Schedule I?

No - for the reasons stated below.

Job Work is an arrangement under which the Principal sends inputs (or capital goods) belonging to him to another person for carrying out any treatment or process assuming accountability for the same with obligation to pay tax and interest if the inputs (or capital goods) are not brought back or supplied from job worker's premises after completion of job work or otherwise, within stipulated time.

Section 143 specifically provides that the inputs (or capital goods) can be sent to job worker without payment of tax. Further, as per the same section, the inputs (or capital goods) shall be deemed to have been supplied by the Principal to the job worker on the day they were sent out to the job worker if the inputs (or capital goods) are not received back or supplied from job workers premises within stipulated time. It can be inferred that till such eventuality, sending of goods to job worker will not be a supply.

Input Tax Credit Rules and Invoice Rules under GST provide that goods can be sent for job work under the cover of delivery challan (& not tax invoice) and where the goods are not returned within the time frame stipulated under Section 143, the delivery challan shall be deemed to be invoice. This supports the inference drawn in the above para.

As such, there would be no liability to pay tax while sending goods on job work even where sent to a related person for job work. In other words, there is no need for treating it to be a case of supply without consideration to related person in view of above specific provisions even considering wide connotation of term 'transfer' used in definition of term 'supply'.

However, the issue of job worker being related person will have to be considered as per Valuation Rule provisions (a) for the value of supply (job work charges) by the job worker and (b) for value of supply of inputs (or capital goods) if eventually not brought back / supplied from job worker premises in stipulated time.

Incidentally, under Central Excise from where the provisions of job work have been adopted in GST, there is no provision that goods should be valued and duty paid when sent to a job worker who is a related person.

B. Inputs sent for job work – is it exempt supply?

No for reasons stated below.

Inputs sent for job work is not a supply attracting nil rate of tax. It is not supply of goods specifically exempted from tax by Notification under provisions of Act. It also does not fall under 'non-taxable supply' i.e. supply not leviable to GST as it is neither the goods excluded from scope of GST nor it falls in category of transactions which are neither a supply of goods nor of services (Schedule III). Hence, value of inputs sent for job work **cannot be regarded as supply of exempted goods**. This was the position under Central Excise.

C. Supply of goods partially using the inputs provided free of cost by the recipient and partially the inputs procured by the supplier himself - will it be treated as job work?

There appears some ambiguity for reasons stated below.

Sometimes arising out of the commercial considerations the arrangement is that the recipient provides some inputs to the supplier without charging him anything for the same and supplier procures other input on his own account to make supply. For example, customer provides component A to supplier free of cost, supplier procures other components B, C & D, manufactures out of A, B, C & D a product Z and supplies the same to customer. The proportion of values of inputs provided by customer and those procured by supplier could vary from case to case. Can supply of product Z be said to be covered under job work? Since it's a composite supply comprising both material and labour, should supplier treat it as supply of goods or as supply of service under job work?

Under Central Excise, such situations were covered under Rule 6 of the Central Excise Valuation Rules. However, in GST, there is no corresponding rule.

The term treatment or process on goods as used in GST has wide scope but in order that a transaction is treated as job work, the treatment or process may have to be on the inputs belonging to the registered recipient/ Principal. Where part of the material, in varying proportions, is procured by the supplier, can it be said to be treatment or process on goods belonging to the Principal to merit treatment as job work? If supplier pays tax only on his value but treating supply of product Z as supply of goods which may be carrying higher rate of tax applying composite supply rule, can customer's supplying component A and supplier's supplying product Z without paying tax on value of component A still fit into job work procedure?

On the other hand, in the example given above, even in the absence of specific rule guided by assumption that it's a case of part exchange, if the customer pays tax on component A and the supplier pays tax including value of component A, since the supplier is not paying customer for component A, the second proviso to Section 16(2) of the CGST Act will bar him from taking input tax credit for the tax paid by customer. This would make the proposition unviable.

There thus appears ambiguity on how such transactions which are quite common are to be dealt with. Under GST the benefit one gets today in sales tax on such transactions (as ownership of

inputs supplied by the customer always continues to vest with him and not transferred to / back from supplier) will be neutralized. But still as a number of such transactions are likely to continue because of commercial considerations, Government needs to come out with proper amendment/ clarification to avoid disputes at later date.

D. Body Building -Will it be covered under job work?

The chassis on which body is mounted / fabricated is supplied by the customer to the body builder. The body builder procures the material required for body and mounts / fabricates the body on the chassis supplied by the customer. The issues are same as under C above.

E. Jigs, fixtures, moulds, dies or tools sent by a manufacturer to another manufacturer for production of goods according to his specifications:

Rule 4(5) (b) of the CENVAT Credit Rules, 2004 allowed CENVAT credit to a manufacturer also in respect of jigs, fixtures, moulds, dies or tools sent by such manufacturer to another manufacturer for production of goods according to his specifications. Thus, the benefit was available even where the arrangement between the two is otherwise not for job work. This was a beneficial provision to avoid CENVAT accumulation at the end of such other manufacturers (usually small manufacturers supplying components to OEMs) and was inserted based on industry representation. There is no corresponding provision under GST and inclusion of such a provision would help the small manufacturers receiving jigs, dies etc. from other manufacturer where they produce the goods according to his specifications but with their own material. Further, like the issue raised under C above, where the dies, tools, moulds, drawings etc. are provided by the recipient to the supplier free of cost (and the supplier makes supply with his material – either partially or fully – thereby not exactly fitting in the definition of job worker), there is no clarity on eligibility to input tax credit in the hands of supplier and also as to whether the supplier is required to recon the value thereof in his supplies by amortization or otherwise. The Government needs to come out with proper amendment / clarification on these issues.

F. Plane view of ‘Job work’ and ‘manufacture’

Under Goods and service tax act, the terms ‘job work’ and ‘manufacture’ have been separately defined under Section 2(68) and Section 2(72) respectively. Schedule II provides the activity of job work and does not touch the concept of manufacture. It shall further be appreciated that though the definitions are limited to specific activity whereas the definition of ‘job work’ presupposes that only activity will be covered under this definition whether the same amounts to manufacture or not. The material sent for job work therefore may be only for processing or complete manufacture. However as per the provisions of Section 143(1) the tax is not payable for goods sent for job work. The service provided by the job worker requires payment of tax as applicable for the services rendered. From this point of view there is no ambiguity in the rates and all the job works will be taxed at 9% CGST irrespective of use. Specific confirmation that the activity of the manufacture can also be covered under job work could help to avoid any ambiguity.

G. Inputs to be sent directly to some other place after job work:

Process is made easier under GST.

Under Central Excise, where the inputs are to be sent after job work to any place other than the factory of the manufacturer sending the inputs, sometimes operational difficulty arises in working under the job work due to requirement as per Rule 4(5) of the CENVAT Credit Rules to receive the inputs or the products produced therefrom back by the manufacturer himself (e.g. where the movement to and again from factory is expensive). In order to overcome this, as an alternative to seeking permission under Rule 4(6) of CENVAT Credit Rules, in situations like where the inputs after processing are to be sent to other factories of the same Company for further use in manufacture, the transactions are done on duty payment (where revenue neutral) instead of the job work. In GST such difficulty should not arise under job work process since as per Section 143 the Principal sending the inputs can supply such inputs, after completion of job work or otherwise, from the place of the job worker itself subject to job worker being registered or Principal declaring the place of business of the job worker as his additional place of business – which would be generally easier to comply.

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- Indirect Taxes Committee