Valuation under GST

DISCLAIMER:
The views expressed in this article are of the author(s). The Institute of Chartered Accountants of India may not necessarily subscribe to the views expressed by the author(s).

The information cited in this article has been drawn from various sources. While every effort has been made to keep the information cited in this article error free, the Institute or any office of the same does not take the responsibility for any typographical or clerical error which may have crept in while compiling the information provided in this article.

Under current regime, each Act under indirect tax whether Central excise, Service Tax, Value Added Tax, Custom Act etc. contains valuation provision with own set of rules which is always riddled in litigation. For instance, works contract service, where supply of goods and services, both are involved, goods are being valued under VAT and services are being valued under Finance Act, which amounts to double taxation, leading to litigation. Supreme Court ruling in the Fiat case which sought to levy excise duty on the cost of manufacture vis-à-vis transaction value, by itself changed the yardstick for measuring the quantum of excise duty.

With the passage of all four bills i.e. IGST, CGST, UTGST, Compensation Cess law and all relevant rules, GST now becomes a reality. Section 15 of the CGST Bill law lays down the valuation aspects under GST which explained the value of taxable supply of goods or services or both on which tax is payable.

It states that the value of supply of goods and services shall be the ‘transaction value’ that is the price actually paid or payable for the said supply, where the supplier and the recipient are not related and price is the sole consideration for the supply. Thus, with the adoption of the transaction value concept, the Government has departed from MRP based method of computation of excise duty. This would be a significant change for the industries supplying products like electronics; footwear, FMCG products etc. who have adopted MRP based valuation for payment of excise duty.

Sec 15(1) defines “transaction value” derives support from the Central Excise Act where one of the conditions is that supplier and recipient are not related persons. In such a case, the question that arises about the value to be adopted under GST in case transaction is between related parties, as any transaction between related persons even without the consideration for furtherance of business would cover under ambit of supply as per schedule I of the CGST Bill. Rule 2 of the “Determination of Value of Supply”, states that the value of supply between related person/distinct person other than agents shall be –

(a) be the open market value of such supply;

(b) if open market value is not available, be the value of supply of goods or services of like kind and quality;

(c) if value is not determinable under clause (a) or (b), be the value as determined by application of rule 4 or rule 5, in that order:

Provided where the recipient is eligible for full input tax credit, the value declared in the invoice shall be deemed to be the open market value of goods or services.

However, if valuation as per the above rule is not determinable, then rule 4 is to be resorted to which envisages that value shall be 110% of cost of production or manufacture or cost of acquisition of such goods
or cost of provision of service. If the value cannot be determinable by rule 4, rule 5 i.e. residuary method is to be followed which envisaged that value shall be determined using reasonable means.

Sec 15(2) explained what are the other items which would form part of the transaction value which includes duties, taxes, amount incurred by recipient on behalf of the supplier, packaging, commissioning, interest, late fee, penalty for delayed payment. Presently, under current regime, interest, late fee, penalty for delayed payment does not attract tax. However, under GST regime, tax would be attracted for which supplier would have to issue supplementary invoice or debit note to collect extra tax on late fee, penalty amount as at the time of raising a tax invoice, supplier will not be in a position to determine whether it would be a delayed payment or not.

Sec 15(3) states that post-supply discount would be excluded from transaction value provided such discounts are established in the agreement and linked to all relevant invoices plus the credit claim on discount value is reversed by the recipient. Practically, all taxpayers supplying goods to the dealer/distributor are offered quantity discount at the end of the financial year once the sales target are achieved by them and same is provided by issuing a credit note. Linking with the relevant invoices is going to pose a major issue because all over the year, dealer/distributor may issues more than 200 or 300 invoices. Further, even in big industries, this quantity discount is not mention in agreement or in some cases there is not agreement at all.

Sec 15(4) states that where the value of the supply of goods or services or both cannot be determined under sub-section (1), the same shall be determined in such manner as may be prescribed.

Further, transfer of goods from factory to depots/branches located in another state is a common phenomenon among the industries i.e. stock transfer. Under current regime, no CST is attracted except excise duty on removal of goods. Under GST regime, the same would be taxable but the valuation to be adopted would be the open market value under rule 2 of the “Determination of Value of Supply” as it would be considered as related party transaction. The question that needs to be addressed here is whether taxing of stock transfer would lead to inverted duty structure. In many MRP based valuation industries, when the goods are transferred to retail outlets and the goods becomes non-moving items, huge discounts are being offered for stock clearance. Since tax is being paid at open market value at the time of stock transfer, it would lead to accumulation of credit on retail outlets.

Further, under current regime, sale of goods through agent, no separate valuation method is being adopted. Excise duty is being charged on the transaction value of the goods. However under GST regime, if the goods are being sold through agent, it would fall under the ambit of “related person” and transaction value cannot be adopted for discharge of GST. In such a scenario, rule 3 of the determination of value of supply is to be resorted which states that value shall be -

(a) be the open market value of the goods being supplied, or at the option of the supplier, be ninety percent of the price charged for the supply of goods of like kind and quality by the recipient to his customer not being a related person, where the goods are intended for further supply by the said recipient;

(b) where the value of a supply is not determinable under clause (a), the same shall be determined by application of rule 4 or rule 5 in that order (as discussed supra).

Clarity in law at the outset will enable easy compliance for the business, at the same time ensure appropriate revenue and avoid frivolous litigation. Although a prompt action by the authorities in bringing the rules
brought a lot of clarity, but still there are hidden issues as each industries have peculiar transaction which will come to know with time.

Acknowledgements

We thank Study Group on Indirect Taxes Kolkata for drafting this article and CA Jatin Christopher for reviewing the same. For any queries, you may connect with CA. Daya Shankar Agarwala at agards@gmail.com.

- Indirect Taxes Committee