Commercial Taxes Department

- 1 NOV 2019

From
Dr. T.V.Somanathan, I.A.S.
Commissioner of Commercial Taxes,
Ezhilagam,
Chepauk,
Chennai – 600 005

To
The Joint Commissioner (ST),
Erode division,
Erode

Letter No. PP1/35346/2019, dated: 24.10.2019.

Madam,

Sub: GST Refund – Inverted Duty Structure for dyeing (Job Work) – Accountant General Audit issues raised – request for clarification to process the refund – regarding.

Ref : 1. Representation from Tvl. Dyers Association of India, Tirupur No. 69/DAT/F.49/2019-20, dated 26.08.2019 and 81/DAT/F.18/2019-20, dated 28.09.2019.

2. The Joint Commissioner (ST), Erode division Roc.No.3768/2019/A12, dated 19.09.2019

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I invite attention to the references cited.

2) The CAG has objected to sanction of refund of ITC accumulated due to inverted tax structure to the job worker suppliers of dyeing services of textile and textile products in Tirupur Division essentially on two grounds:

a. The classification related to manufacturing services on physical inputs (goods) owned by others, viz., 9988, has been adopted by the suppliers of dyeing and bleaching services as job workers attracting 5% GST, which is incorrect. Had the services of job work of dyeing, bleaching, etc., been classified correctly under 9997 (other washing, cleaning, dyeing services nowhere else classified) which attracted a tax of 18% GST, inversion itself

would not have occurred and refund would have been unwarranted. Further, in the instant case, the refund was not pertaining to the value of service portion alone but also pertained to the physical inputs (goods) valued more than 50% of turnover of the suppliers were of their own purchase.

b. Since there is no definition of 'output' (as mentioned under S.54(3)) under GST Acts, the dictionary meaning of output which indicates only to supply of goods only needs to be taken. The formula for computing net ITC also does not include inputs during the period using the same analogy. Therefore, the jobworkers who are service providers are not entitled for refund on account of Inverted Tax Structure, which is restricted to only suppliers of goods.

3. With respect to the first ground of objection, it is seen that it has two limbs; one pertaining to misclassification and second pertaining to valuation of job work services. They are discussed as under:

As per S.2(72) of the GST Acts, "manufacture" means processing of raw material or inputs in any manner that results in emergence of a new product having a distinct name, character and use and the term "manufacturer" shall be construed accordingly.

As per S.2(68) of the GST Acts, "jobwork" means any treatment or process undertaken by a person on goods belonging to another registered person and the expression "jobworker" shall be construed accordingly.

Sl.No.3 of the Schedule II declares any treatment or process which is applied to another person's goods as a 'supply of services'.

On a combined reading of the above, it will appear that jobwork which is nothing but a treatment or process on another person's (goods of 'principal' as referred in S.143 of the Act) goods is deemed to be a supply of 'services' and further would fall under the activity of 'manufacturing services'.

SAC 9998 covers 'manufacturing services' on physical inputs owned by others going by the explanatory notes issued by the CBIC based on United Nations Central Product Classification (UNCPC) (CAG team also quotes the same).

It obviously flows that job work naturally gets covered under the service accounting code 9998, and more so under 998821, being a specific description for 'Textile manufacturing services'.

Regarding the contrary contention of CAG Audit that services like bleaching, dyeing, etc., on textiles and textile products would fall under 9997, it is submitted that on a cursory glance of the illustrative list of services, it would easily appear that all types of laundry services and value added services anciliary or incidental to such washing, or cleaning services pertaining to made up textile articles and apparels for personal use are only covered under the 'other services' detailed under 9997. Further, the service code 999715 pertaining to dyeing and colouring services is specifically described to include dyeing and colouring of apparels and other textile articles, NOT IN CONNECTION WITH PRODUCTION OF SUCH ITEMS (capitalization supplied). This exclusion has been specifically provided to clear out any artificial confusion that may arise in minds of the reader regarding the differences between manufacturing services like dyeing, bleaching, etc., and the superficial services of cleaning and laundry services for textile articles, etc., which may include dyeing, etc. The dyeing services for household or enterprise collective textile articles are NOT to be equated with the textile finishing services like bleaching, dyeing, etc., which are necessarily 'manufacturing services'. The audit's finding that the residual entry 999719 (other washing, cleaning and dyeing services, not elsewhere classified) would cover the dyeing and bleaching services done as jobwork for the textiles and textile products is far from the truth. When all the groupings under 9997 pertain to a specific service cluster of services pertaining to laundry services and other allied services, the residual entry alone cannot be dragged to cover the manufacturing services of dyeing, bleaching, etc.

Notwithstanding the above reasoning, assuming without accepting, that the service of dyeing or bleaching is capable of a differential treatment for any purpose based on its description, the most specific description shall have to be preferred over a more general description as per the principles of interpretation in the explanatory notes. When the 'manufacturing services' under 9988 cover a wide variety of services like textile finishing services, textile manufacturing services, specific to textiles and

other industrial sectors involving production of goods, which include bleaching, dyeing, etc., an entirely different services set falling under 9997 pertaining to auxiliary services under the gamut of laundry services, cannot be equated to such manufacturing services by any yardstick, merely due to an occurrence of a single word 'dyeing' mentioned under 9997. Infact, there are quite a few services who are capable of being fitted into any heading but the guide should be what is apt and suitable for the specified service based on the activity and context and not merely to be led by semantics.

The above argument is reinforced by the fact that a concessional rate of tax at 5% was specifically carved out for the jobwork services pertaining to textile and textile products (para 13.2 of minutes of 20th GST Council meeting) among other job work services. The services of dyeing, etc., as a job work process pertaining to textile sector also finds separate mention in the annexure 1 to the agenda volume 2 of the same meeting (proposals found acceptable by the FITCOM). Subsequently a notification no. 20/2017-CT (Rate) dated 22/8/2017 (G.O. (Ms) No. 94 dated CT & Regn. 22.08.2017 Notification No.II(2)/CTR/668(d-1)/2017, dated 22.8.2017 [Issue No. 274]) was issued to give effect to the GST Council's approval to the proposal to reduce the rate of tax for the job work services for textile sector by way of inserting an entry for services by way of job work in relation to textiles and textile products falling under Chapter 50 to 63 in the First Schedule to the Customs Tariff Act, 1975. Thus all job work processes like dyeing, bleaching, etc., pertaining to textiles and textile products attracted 5% rate of GST from 22/8/2017.

Therefore, there was no occasion for misclassification in respect of services pertaining to the job work processes in the textile sector except to classify under 9988 as established by the above reasons. Of course, this naturally resulted in an inverted tax structure for the job workers of textiles sector, if they had purchased inputs leviable to a rate of tax higher than that of 5% which was the prescribed rate of tax from 22/8/2017 for the jobwork processors (manufacturing services) of textiles and textile products owned by the principals.

With regard to the suppositions of the CAG audit that service value does not include the value of inputs procured by jobworkers in order to provide the services of dyeing or bleaching processes, etc., it is submitted that it is common knowledge and normal trade practice that jobwork charges will always include all costs of labour, any inputs used for performing the jobwork and other costs incurred in carrying out the jobwork process. Further, vide circulars no.38/12/2018 dated 26/3/2018 and 88/07/2019-GST dated 1/2/2019 issued with the approval of GST Council under S.168 of the Act, the GST Policy Wing, while deliberating on valuation of jobwork services, had categorically stated that ".....The value of services would include not only the service charges but also the value of any goods or services used by him for supplying the jobwork services, if recovered from the principal...." (para 9.4(i)). This principle is in consonance with the provisions of Section 15 of the GST Acts and therefore, on no count, the surmise of the AG Audit's contention that service value alone has to be counted for the purpose of any refund (whether arising out of inverted duty structure or anything for that matter) cannot be correct.

Once the provisions of S.15, the governing section for value of supply have been adhered to, as emphasized by the circulars cited above, it is immaterial that the value of inputs purchased by the jobworker and used for carrying out the jobwork process is more than 50% of his total turnover or falls under some artificial threshold limit of usage of his own inputs while processing the goods of the principal. There is no logic nor law backing the argument of the audit.

4. With reference to audit's other point to deny refund that only suppliers of goods and NOT TO SUPPLIERS OF SERVICES are eligible for refund of accumulated ITC due to inverted tax structure, it is submitted that during the discussion in the 27th meeting of the GST Council, *Commissioner (GST Policy Wing), CBIC had stated that Section 54(3)(ii) of the CGST Act, 2017 does not allow for refund of taxes on account of inverted duty structure in case of input services, whereas, there is no restriction to avail the refund where the outward supply is that of services, Rule 89(5) of the CGST Rules needed to be amended to modify the formula for calculating Maximum Refund Amount according to the Act. After discussion, GIC agreed to the following: Amend the Rule 89(5) of*

the CGST Rules as below (indicated in underlined italics and italics strikethrough mode). Maximum Refund Amount = {(Turnover of inverted rated supply of goods and services) x Net ITC÷ Adjusted Total Turnover} - tax payable on such inverted rated supply of goods and services Explanation: For the purposes of this sub-rule, the expression:- (i) "Net ITC" shall mean input tax credit availed on inputs and input services during the relevant period other than the input tax credit availed for which refund is claimed under sub-rules (4A) or (4B) or both; (ii) "Adjusted Total Turnover" shall have the same meaning as assigned to it in sub-rule (4). 4.3.4. Accordingly, Notification No. 21/2018 – Central Tax was issued on 18 April 2018 (agenda item 2)

5. Further, in the 28th meeting of the GST council, *Commissioner, GST Policy Wing, CBIC had stated that rule 89 (5) of the CGST Rules was amended vide notification No. 21/2018 – Central Tax dated 18.04.2018 wherein the words "services" was included in the formula given for computing the maximum amount of refund on account of inverted duty structure. Under the CGST Act, refund of ITC on account of inverted tax structure was always available on output supplies of services and vide the said amendment to rule 89(5), it was only sought to clarify the same. However, the said amendment was effective from 18.04.2018 i.e., the date of the publication of the said notification in the Official*

constitutional body, i.e., GST Council which had approved the amendment to the rules after elaborate discussions.

7. In fine, the audit's objections are not found to have any rational basis to be accepted and accordingly, the same may be replied to as 'not acceptable' for the reasons mentioned above.

8. *In the light of the above decision, you are also advised to inform the ACs under your control to proceed to deal with the refund claims on merits without linking to the audit's preliminary objection so that the trade do not suffer.*

9. Further, no pre-emptive or collateral action need to be taken by the jurisdictional officers to demand the refund already granted, merely based on the audit slips issued by the CAG team and any action initiated by officers to recover the refund already sanctioned, may be advised to be withdrawn or kept in abeyance.

Sd/-Dr.T.V.Somanathan
Commissioner of Commercial
Taxes

//Forwarded by Order//

Assistant Commissioner (STC)