



ADVAITA LEGAL
ATTORNEYS AND
ADVOCATES

Key Indirect Tax Risks on PPP infrastructure projects

Sudipta Bhattacharjee

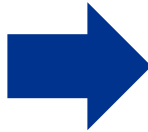
Partner – Tax Controversy Management & Contract Documentation

December 15, 2017



Rights over underlying 'Immovable Property' and constructed assets thereon

Nature of right over underlying immovable property- Critical factor in determining tax liability



In Infra projects awarded on PPP basis, nature of rights over underlying land varies from model to model (BOOT v. BOT/DBFOT). Many Concession Agreements are on **DBFOT basis**

- ❖ Land will be given to Concessionaire by way of lease/ license - whether Concessionaire can be the owner (under general law) of the assets constructed on land not owned by Concessionaire
- ❖ **Established principle:** Unless there is a contract to the contrary, the ownership of any superstructure constructed over the leased land by the lessee (during the lease) would revert to the lessor (owner of the land) on termination of the lease
- ❖ Section 108 (d) of the Transfer of Property Act, 1882 reads as below:
 - “In the absence of a contract or local usage to the contrary, the lessor and the lessee of immovable property, as against one another, respectively, possess the rights and are subject to the liabilities mentioned in the rules next following, or such of them as are applicable to the property leased....*
 - (d) If **during the continuance of the lease any accession is made to the property, such accession (subject to the law relating to alluvium for the time being in force) shall be deemed to be comprised in the lease**”*

Rights over underlying 'Immovable Property' and constructed assets thereon (CONTD.)

- ❖ To elucidate, if any house is built on leasehold land, the lessee will have a leasehold right on the house just as it has a leasehold right on the land and the house shall revert to the lessor (ie the owner of the land) on termination of the lease, unless there is a contract to the contrary

- ❖ **Therefore, in order to ensure that the person who constructs over a leasehold land must also have ownership rights over the constructed assets, it is necessary that arrangement between the Lessor of the land and the Lessee, clearly provides for it**
 - Example – **NHAI concession agreement has no such provision.**

 - Model concession agreement for **Greenfield Airports also does not seem to have such a clause.**
Clause 10.2.4:

“10.2.4 It is expressly agreed that the licence granted hereunder shall terminate automatically and forthwith, without the need for any action to be taken by the Authority to terminate the licence, upon the Termination of this Agreement for any reason whatsoever. For the avoidance of doubt, the Parties **expressly agree that notwithstanding any temporary or permanent structures erected on the Site by the Concessionaire or its sub-licensees, the licence in respect of the Site shall automatically terminate, without any further act of the Parties, upon Termination of this Agreement”**”

Rights over underlying 'Immovable Property' and constructed assets thereon (CONTD.)

- ❖ ***Thus, as a thumb rule, if the land on which the proposed project is to be carried out/the Project Assets is owned by the Concessionaire, then Concessionaire is not undertaking a works contract and is instead the contractee/employer/ project owner***

- ❖ One cannot render 'service'/ 'works' to oneself - To have "service", there must be a "service provider" rendering services to some other person(s), who shall be recipient of such "service"
 - If Concessionaire owns the land and/or Project Assets, Concessionaire is constructing for itself - no service being rendered;

 - **If Government Nodal Agency owns the land and/or Project Assets, service/ works is being rendered to Government Nodal Agency by Concessionaire**

- ❖ ***IF THE CONCESSIONAIRE IS NOT A "PROJECT OWNER", then following tax issues arise:***
 - If the concessionaire is not a project owner, is he carrying out a 'works contract service' as understood under GST laws and thereby liable to pay GST?;

 - Would the input side GST collected from such concessionaire by its contractors be available as credit against above-mentioned output side GST?

Rights over underlying 'Immovable Property' - a relevant judicial precedent

M/S Ashoka Infrastructures v. State of Maharashtra (2014-VIL-12-MSTT)

Whether the contract taken up by the appellant could be said to be works contract and whether he could be said to be dealer as envisaged under Maharashtra Sales tax on Transfer of Property in Goods Involved in execution of works contract (Re-enacted Act, 1989 (Act) and liable to pay tax on the turnover of sales in respect of the goods used at the time of the road construction?

Facts:

- ❑ BOT project agreement was entered on 28.08.1997- agreement was for a period of 8 years and 9 months.
- ❑ Appellant was given right of collection of toll, expenditure incurred by them was to be recovered by way of toll during the concession period and upon completion of the lease was to hand-over the property back Government free of cost

Judgment:

- ❑ Section 2(d) of the Act- essential ingredients (i) He has to be a person.(ii) Whether they work for valuable consideration, commission, remuneration or otherwise.(iii) The person transfers property in goods involved in the execution of works contracts
- ❑ Handing over the project free of cost is after the concession period is over, as it is deemed that entire cost of the project, inclusive of interest and expenses and profits have been realized. Therefore, contention of the appellant that he is not earning any profit cannot be accepted -All the ingredients of dealer are satisfied.
- ❑ Appellant is a legal person. There is valuable consideration which has passed. There is transfer of property in goods involved in works contract. Hence, he is a dealer
- ❑ Hence, B.O.T. project involves both goods, labour and services and therefore, it is a works contract - Once it has been held that appellant is a dealer what is required now for him is to pay tax on the turnover of sales in respect of goods
- ❑ Reliance was placed on Kone Elevators India Pvt. Ltd. Versus State of Tamil Nadu and others reported in [2014] 71 VST 1 (SC) and other cases.

Credit restriction on 'Works contract' under the GST

- ❖ **Restriction imposed on availment of ITC of GST paid on inputs/input services availed in supplying the works contract services for construction of immovable property –**
 - “(c) works contract services when supplied for construction of an immovable property (other than plant and machinery) **except where it is an input service for further supply of works contract service**”*

- ❖ **Consequently, no ITC is available of the inputs/input services used in providing the aforesaid 'works contract services' – However, following exceptions are carved out –**
 - **Where such services are input services for further supply of works contract service;**
 - **Where the immovable property qualifies as 'plant and machinery'**

- ❖ **Plant & Machinery defined to mean:**

apparatus, equipment, and machinery fixed to earth by foundation or structural support that are used for making outward supply of goods or services or both and includes such foundation and structural supports **but excludes –**

 - i. Land, building or any other civil structures;
 - ii. Telecommunication towers; and
 - iii. Pipelines laid outside the factory premises

Impact of Concessionaire qualifying as 'works contractor'/'owner' - applicability of credit restriction on 'Works contracts' under GST

IF CONCESSIONAIRE IS TREATED AS 'PROJECT OWNER':

- ❖ Companies which undertake the **development of port** for providing port services, **cannot avail the ITC of the GST paid on inputs/input services**
- ❖ Companies engaged in PPP in Railways
 - **Whether 'railway track/line' would qualify as an 'immovable property'?**
 - **If yes, then no ITC** would be allowed, else, ITC will be allowed
- ❖ Companies engaged in the **construction of road**, will also have the **same fate** with respect to availment of ITC
- ❖ **Thus, the credit restriction would result in significant increase in the working capital for the companies engaged in infrastructure projects**

IF CONCESSIONAIRE IS TREATED AS IF PROVIDING SERVICES TO THE NODAL AGENCY:

- ❖ **No credit restriction as per above. But how to determine output GST liability? 'Consideration' will be received over 20/25 years!**
- ❖ Pursuant to the 22nd GST Council Meeting dated 06.10.2017, the Government vide Notification No. 32/2017 – Central Tax (Rate) dated 13.10.2017, has provided for **GST exemption for annuity paid by NHAI** (and State authorities or State owned development corporations for construction of roads) to concessionaires for construction of public roads

Impact of GST on Concession Agreements – ‘change in law’

- ❖ For example, there are NHAI contracts that have been entered into the Pre-GST Regime whereby annuity payments had been calculated and factored considering Service Tax exemptions. Since GST is applicable at the rate of 12%, it is important to invoke ‘Change in Law’ clause under such concession agreements
- ❖ Concession agreements prescribe **Materiality Thresholds** in any accounting year for adjustment of any increase in costs, reduction in net after tax return, or other financial burden **as a consequence of change in law**
- ❖ Broad principle provided for computing the financial impact of change in law i.e. impact to be offset **should put the affected party in same position as if the change in law has not occurred**
- ❖ **HOW TO ESTABLISH IMPACT OF ‘CHANGE IN LAW’?** Methodology of computing of impact of change in law/ taxes typically not prescribed under the Concession Agreements – circulars issued by Nodal Agencies like NHAI to deal with this may not be suitable



ADVAITA LEGAL
ATTORNEYS AND
ADVOCATES

THANK YOU

Delhi

703-706

International Trade

Tower, E Block

Nehru Place

New Delhi 110019

Tel +91 11 3323 2700

Fax +91 11 30671304

Key Contacts

sujitghosh@advaitalegal.com

sudiptab@advaitalegal.com

Mumbai

Lodha Excelus, 1st Floor,

Apollo Mills Compound,

N.M. Joshi Marg,

Mahalakshmi,

Mumbai 400 011

Tel +9122 39896000

Fax +91 22 39836000

Disclaimer: Pursuant to the Bar Council of India rules, we are not permitted to solicit work and advertise. You, the reader acknowledges that there has been no advertisement, personal communication, solicitation, invitation or inducement of any sort whatsoever from us or any of our members to solicit any work through this newsletter. The information provided in this newsletter is solely available at your request and is for informational purposes only, it should not be interpreted as soliciting or advisement. We are not liable for any consequence of any action taken by the reader relying on material/ information provided in the newsletter. In cases where the reader has any legal issues, he/she must in all cases seek independent legal advice. Any information obtained or materials used from this newsletter is completely at the reader's volition and any transmission, receipt or use of the contents of this newsletter would not create any lawyer-client relationship.

© 2017 Advaita Legal. All rights reserved.



**SUDIPTA
BHATTACHARJEE**
**PARTNER, ADVAITA
LEGAL**

703-706,
INTERNATIONAL
TRADE TOWERS,
NEHRU PLACE, NEW
DELHI

T: +91 11 3323 2752
(DIRECT)

M: +91 93507 34337

E: sudiptab@advaitalegal.com

Professional and industry experience

- Sudipta is a Partner at Advaita Legal and has more than 12 years of experience in tax and legal advisory services to clients in diverse sectors and in structuring, drafting, reviewing, and negotiation of various contracts.
- Sudipta specializes in all indirect taxes as well as contract documentation related services. He has been involved in providing strategic tax and contract-review related advice vis-à-vis India's first national waterway project as well as India's first ultra-mega power project.
- He has a rich, practical & varied experience in advising various clients in the realm of taxes during the contract formation as well as the implementation stage.
- He has played a key role in conceptualizing the overall transaction structures, finalizing the relevant contractual documents and tax impact analysis for several projects.
- Advisory *vis-à-vis* effective resolution of high-stake tax/commercial disputes in the realm of contracts including with respect to alternate dispute resolution mechanisms in commercial contracts and representing clients in alternate dispute resolution mechanisms before appropriate bodies.
- He has been listed by the **International Tax Review** as an '**Indirect Tax Leader**' for the year 2017-18.
- He has worked with Reliance and BMR in his earlier stints. In his stint with Reliance, Sudipta was involved with respect to structuring, negotiation and finalization of various high-value procurement contracts as well as other commercial contracts including claims management.