



Impact of Kerala Flood Cess –GST

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Introduction and background

In August 2018, the State of Kerala faced a devastating flood due to high rainfall which was the worst flood in nearly a century. There was huge loss to the assets, revenue of the State. As a result, the State of Kerala proposed for levy of additional cess in GST which was approved by the GST council in its 32nd Council meeting held on 10th January 2019. The council approved the proposal of State of Kerala to mobilise the revenue through levy of additional cess on intra-State supplies within the State of Kerala at a rate not exceeding 1% for a period not exceeding two years. The question which arises is that in terms of Article 265 of the Constitution of India, whether the GST Council has the jurisdiction to impose an additional tax on the same supply. If the answer is in the affirmative, then many States reeling under water shortage, drought, famine, tsunami, earthquake etc. could also go for additional taxes and the pristine principles of GST of fewer rates would be defeated.

Levy of Kerala Flood Cess

After the approval in GST council meeting, for the purpose of rebuilding, reconstructing, rehabilitating and compensating the State from such disaster, the Kerala State vide its Finance Act 2019 introduced a new levy of Kerala Flood Cess (herein referred as “KFC”) on specified intra-State supplies made by a taxable person as provided under section 9 of Kerala State Goods and Services Tax, 2017(herein referred as “KSGST”). Though initially planned to levy from 1st April 2019, the levy has been made effective from 1st August 2019 for a period of two years due to few challenges in respect of such introduction. The levy of flood cess would be continued till 31st July 2021 (assuming the effective date would not get deferred anymore).



The levy of KFC would be applicable on all intra-State supplies within Kerala **except** for the following transactions:

- i. Supplies made by a person who has opted for composition levy under section 10 of KSGST;
- ii. Exempted supplies as notified under section 11 of KSGST;
- iii. Supplies made by a registered taxable person to another registered taxable person i.e. b2b transaction;
- iv. Supplies of **goods** which are taxable @ 0.125% under KSGST;
- v. Supply of **goods or services** which are taxable @ 2.5% as notified under KSGST;

Since the levy of KFC is limited to intra-State supply within the State of Kerala, inter-State supplies would not suffer any such cess. The suppliers of any goods / services from other States to Kerala customers would also not be required to pay such cess.

The above cess would be applicable at the following rates on intra-State supplies:

Sl. No.	Description of goods/services	Rate of KFC
1	Goods/ services exempt u/s 11 of KSGST, 2017	Nil
2	Goods liable @ 0.125% under KSGST, 2017 (i.e. diamonds)	Nil
3	Goods or Services liable @ 2.5% as notified under KSGST, 2017	Nil
4	Supplies made by a composition dealer registered under section 10 of KSGST, 2017	Nil
5	Supplies made between registered persons	Nil
6	Goods liable @ 1.5% under KSGST, 2017 (i.e. precious metals like Gold)	0.25%
7	All other goods and services	1%

The provisions of KSGST, Central Goods and Services Tax Act, 2017 (herein referred as "CGST") and rules made thereunder in relation to definitions, authorities, assessment, audits, non-levy, short-levy, interest appeals, recovery of tax, offences and penalties, shall, as far as may be, apply for levy and collection of the cess.



Kerala Flood Cess Rules, 2019 (KFCR)

In exercise of power conferred under section 14 of Kerala Finance Act, 2019 Government of Kerala had made rules called “KFC Rules, 2019” which provides the levy, collection of cess and the process and format for filing monthly return for flood cess through the official portal of Kerala Government www.keralataxes.gov.in where the liable assessee has to create his own account for filing returns.

The major impact of KFC would be on the intra-state b2c (i.e. to unregistered person) suppliers where the suppliers can't plan or restructure their transaction to get escaped from the levy of KFC like accommodation services, residential complex constructions, transportation services (other than exempted), tourism services, and other consumer-oriented supplies. However, the flood cess are not levied on exempted supplies and **supply of goods or services** which are taxable @ 2.5% as notified by KSGST.

By introduction of levy of flood cess the price of the products and services would tend to increase.

Valuation principles for KFCR

The flood cess would be levied on the value determined under section 15 of KSGST. In terms of section 15, the value of a supply of goods or services or both would be the transaction value, which is the price actually paid or payable for the said supply of goods or services or both where the supplier and the recipient of the supply are not related and the price is the sole consideration for the supply.” It includes any taxes, duties, cesses, fees and charges levied under other laws (other than GST law) if charged separately by the supplier. However, the flood cess levied would not be included in the value as per Rule 32A of Kerala State Goods and Service Tax Rules, 2017. For example, if the value charged by the supplier is `1,00,000/- and GST is levied @ 18%. Cess and GST amount to be paid for the supply is calculated as below:-



Sl. no	Description	Amount (₹)
1	Value of Supply	1,00,000
2	KFC @ 1% on value of supply	1,000
3	GST @ 18% on value of supply	18,0000
4	Total Invoice Value	1,19,000

**FAQ issued
by the State**

In reference to
the levy of

additional cess, the State of Kerala has issued FAQ on 29th July 2019 to clarify the doubts in relation to levy of KFC. However, there are some answers provided in the FAQ which are not in line with the KFCR and Finance Act, 2019 which are discussed below:-

i. Transaction between registered persons:

In terms of the Finance Act, 2019 and the KFC rules, 2019, the KFC would not be levied on supplies between the registered persons. The definitions of CGST and KSGST Act where registered person includes a person registered under section 25 of CGST/KSGST Act squarely applies to the flood cess rules as per section 14(4) of Finance Act, 2019 and rule 7 of KFC rules, 2019.

However, question no.21 in FAQ has an answer in contrary wherein it has been stated that flood cess would be applicable for a supply made to a registered person outside Kerala, if the place of supply falls within Kerala. This seems to be against the provisions which clearly states that exemption is for supplies to registered person without any mention on place of supply or State of registration. Such clarification could have been issued considering only the provisions of KSGST Act 2017 which defines the 'registered person' as person registered under Section 25 of KSGST Act. As per the Finance Act and KFC rules, there is no such discrimination made between registered person within Kerala and outside Kerala. The intention of State might be to levy additional cess on



such transactions where the recipients are not eligible to avail the input tax credit. However, the same is not reflected in the Finance Act and KFCR.

ii. Flood cess on transaction held not in the furtherance of business:-

In terms of section 14 of Finance Act, 2019 and KFC Rules 2019, the cess would be levied on specified intra-State supplies to unregistered persons (exemption to registered persons) within Kerala and the definition provisions would be squarely applicable from the CGST / KSGST Act, 2017.

In terms such law, in order to be covered under supply, it has to be made in the course or furtherance of business by the supplier. The intention of buyer of goods /services should not make any difference in such levy. It could be for his business / non-business use. Exemption should be available to supplier if the buyer is registered.

However, Q.12 & 18 in FAQ have been answered in such a way that, if the transaction occurs **not in** the furtherance of business, flood cess would be applicable even if the transaction is with registered buyer.

The term “business” has a broader meaning and specifically defined under section 2(17) of CGST / KSGST and would be different from definition of “business” under Income Tax Act. In terms of GST there is no requirement of regularity, frequency, volume, profit motive in order to fall within the ambit of business. Moreover, the word ‘furtherance’ has a very wider coverage. It covers even advancement, development, betterment, helping, backing, promotion etc. Such test has to be made from the perspective of the supplier and not the recipient/ buyer.

FAQs need not be relied on when it is not in line with the law. The tax payers could approach the GST Council through representations.



Business disparity in State

The levy of cess on intra-State supplies would create disparity in the value charged for supply of services to unregistered customers between the services providers within the State and outside the State. For example, tour operators incorporated within the State of Kerala has to charge flood cess whereas tour operators incorporated outside Kerala are not required to charge flood cess to their unregistered customers as it would be an inter-State supply.

Due to this, there could be a possibility for multiple GST registration holders to shift their invoicing/ supply of services from Kerala to other States to avoid levy of extra cess of 1%. Even the exemption from cess to composition dealers could also create a disparity between the composition suppliers and normal suppliers. Following brief analysis could be helpful in understanding the impact/ issues for some of the supplies:

Chartered Accountancy services

Being the income tax filing due date extended till 31st August 2018, the invoices raised on or after 01st August 2019 for tax payers who are unregistered persons under GST would suffer flood cess @ 1%. There is a space for planning of transaction by receiving advance from clients before 01st August 2019 and make the time of supply of the transaction fall before 01st August 2019 in order to escape from such levy of flood cess. Further, it would reduce the fees charged to the client i.e. his cost.

Moreover, Chartered Accountants from the neighbouring States would have lower cost.

Construction Services

The major customers to the construction service are unregistered individuals, the majority of the transactions of such construction service providers would attract the levy of KFC. However, the levy attracts on supplies made from 01st August 2019 as it is the effective date of levy for flood cess. Hence, where the time of supply (date of



completion of event / date of receipt whichever is earlier) falls on or after 01st August 2019 flood cess has to be levied by the builder in the consideration (exclusive of GST).

Hence payment of instalment by the customer to their builders before 01st August 2019 might reduce their instalment amount by 1% and the amount can make a huge difference to the buyer. For instance, if the instalment amount sums to `10 lakhs if such amount is paid before 01st August 2019 the amount sums to `10 lakhs + GST (may be either inclusive or exclusive). However, if the same is paid on or after 01st August 2019 the instalment amount may increase up to `10,000/-(1%) comparing to the previous. Further, the customers may postpone their investment plan of purchasing houses/ flats for next two years where they can avoid paying additional cess of 1%. Since the 1% of the value of the property would make huge difference to common man. For instance, if the property values `1 crore/-, the customer ends up paying extra `1 lakh/- as KFC if he purchases the flat between 01st August 2019 till 31st July 2021.

Accommodation services

In terms of section 12 and 13 of IGST Act, the place of supply for services in relation to an immovable property would be the actual location of such immovable property or its intended location. Hence 99% cases of accommodation services would fall under intra-State supply as the location of the supplier and the place of supply would more likely fall within the State. Hence there would be sure increase in the cost of accommodation in hotel industry, which can impact the tourism industry as the place of supply to house boats would be same as an immovable property.

Motor Vehicle dealers

The flood cess would even impact motor vehicle and its incidental services supply as the major transactions are of nature b2c. However, the business has to ensure the place of supply for each transaction to analyse whether flood cess would be levied or not. If the delivery of the vehicle to customer terminated within Kerala then it amounts to intra-State supply and flood cess would be attracted.



In case of vehicle servicing, the place of supply has to be identified for spare parts supply and servicing portion. For service portion the place of supply would be location of the service recipient i.e. either registered place of business or usual place of residence where in relation to spare parts, the place of supply would be the place the delivery is terminated to the customer.

Hence, identifying the applicability of levy of flood cess in the business would require analysis of the transaction case to case based on the followed business practices.

Conclusion

The intention of law is to levy additional cess on supplies to unregistered customers to rebuild the State. There are certain pros and cons in the levy as there could be attempts in restructuring of transactions by the tax payers such as shifting the invoicing to other States to covert the intra-State supply to inter-State supply to avoid payment of extra cess. Further, a person may also postpone his investment for purchasing flats for next two years to avoid paying KFC. Certain services where the transactions would be intra-State supplies like accommodation services, construction services, restaurant services etc., would become cash cows to the State to collect the flood cess. The levy can also have impact on tourism industry. We are sure that the State government would have considered all these factors before proposing such levy. Tax payers are suggested to comply with the new rules including filing of monthly returns in form KFC-A.

Special thanks to CA Mahadev for penning this article. For any further queries/comments please write us to arjun@hiregange.com, mahadev@hiregange.com, madhukar@hiregange.com.

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