



## REVERSE CHARGE – A SNEAK PEEK

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In the normal course of business, the taxes are paid by the buyer, and the seller collects the taxes and remits the same to the tax authorities. This method of tax collection or levy is known indirect taxation. In cases when the person who derives any income like salaries, he pays the taxes directly, and it is known as direct taxes. There are few cases when the buyer pays the tax on behalf of the seller and such tax is known as reverse charge or use tax or self-assessed tax. Governments across the globe opt for reverse charge for the following reasons

- a) To identify the business which from unorganized / unregistered taxpayers
- b) To ensure that all transactions also falling under the tax net
- c) To help them to make decisions with the tax laws as to bring in more products/services under tax net or reduce tax rates etc.,

The treatment or the process of payment of taxes under reverse charge is of two types:

- i) The buyer of the goods or services have to pay the tax first in cash and then utilize same for making payment of other taxes, i.e., availing input tax credit
- ii) There is no actual requirement to pay taxes directly, only an accounting entry for the tax liability and utilization / recovery is done

In all the case wherever reverse charge is applicable, the reporting has to be done separately either at the transaction level or in summary level in the various returns to be filed.

We had reverse charge in India under Service tax for inward supplies on a classified list of services and in VAT also few states have adopted reverse charge. Goods and Service Tax is introduced in India from 1<sup>st</sup> July 2017, and the basic idea is to increase the tax base of the taxpayers. In order to bring the transactions/

business in the unorganized sector to the organized sector, reverse charge has been introduced for goods and services in GST, unlike the erstwhile taxation where it was applicable only to services.

Reverse charge has been defined in Sub-section 98 of Section 2 of the CGST Act as “means the liability to pay tax by the recipient of supply of goods or services or both instead of the supplier of such goods or services or both under sub-section (3) or sub-section (4) of section 9, or under sub-section (3) or subsection (4) of section 5 of the Integrated Goods and Services Tax Act”.

Reverse Charge in GST is applicable in the following two cases

- a) When goods or services or both procured from unregistered taxpayers
- b) For the specified list of goods and services notified by the government on recommendations of the GST Council.

Point “a” is referred in Sub-section 3 of section 9 of the CGST Act and point “b” is referred in Sub-section 4 of section 9 of the CGST Act.

As reverse charge is also applicable for supplier of goods under GST and the supplier of goods registered under the erstwhile regime Central Excise or VAT are not aware of it completely to provide some time for their understanding and implementation, the government has given a provision that reverse charge will be applicable only if the inward supplies is above Rs 5,000 per day wide Notification No 8 /2017 – Central Tax (Rate) dated 28<sup>th</sup> June 2017.

As reverse charge is a new concept and many of the small and first-time taxpayers were not able to understand and the adopt the same. Many representations have been received by the government for differing/deletion of this provision.

Basis on these, in the 22<sup>nd</sup> GST Council Meeting, held on 6<sup>th</sup> Oct 2017, the GST Council has taken a decision to differ the reverse charge provisions on the inward supply of goods or services from the unregistered taxpayers till 31<sup>st</sup> of March 2018. The same was notified wide Notification No 38/2017 – Central Tax dated 13<sup>th</sup> Oct 2017.

The said notification is only for the inward supply from the unregistered taxpayers only, meaning that the provisions of Sub-section 3 of Section 9 of the CGST Act will be applicable for the inward supply of notified goods or services. It also means that the inward supplies from the unregistered taxpayers will not be liable for reverse charge till 31<sup>st</sup> Mar 2018.

*G.S.R. (E).- In exercise of the powers conferred by sub-section (1) of section 11 of the Central Goods and Services Tax Act, 2017 (12 of 2017), the Central Government, on being satisfied that it is necessary in the public interest so to do, on the recommendations of the Council, hereby makes the following amendment in the notification of the Government of India, in the Ministry of Finance (Department of Revenue), No.8/2017-Central Tax (Rate), dated the 28th June, 2017, published in the Gazette of India, Extraordinary, Part II, Section 3, Sub-section (i), vide number G.S.R. 680(E), dated the 28th June, 2017, namely:-*

*In the said notification, the proviso under Paragraph 1 shall be omitted*

*2. The exemption contained in the notification No. 8/2017-Central Tax (Rate) dated the 28th June, 2017 as amended by this notification shall apply to all registered persons till the 31st day of March, 2018.*

A careful review of the notification No 38/2017 – Central Tax dated 13<sup>th</sup> Oct 2017 we observe that there is no usage of the words “Retrospective,” it means that the notification is from a perspective in nature. Moreover, till date, all the notifications issued under GST for rate change or for LUT or additions of items under reverse charge are not in a retrospective in nature.

The taxpayers have to consider all the transaction, i.e., on inward supplies from the unregistered taxpayers till the date of Notification No 38/2017 – Central Tax dated 13<sup>th</sup> Oct 2017, compute reverse charge accordingly, account it, report it in GSTR – 3B for the month of October and pay the reverse charge liability. Once the reverse charge liability is discharged, the input tax credit can be availed and utilized it for the payment of GST liability.

All such transaction summarized and reported in GSTR – 3B have to be shown in GSTR -2 for the month of October 2017.

This notification is only perspective in nature and not retrospective in nature.

A sneak peek on reverse charge/use tax across the globe

### **1. United States of America**

In America Use tax compliments the Sales Tax. Use tax is normally levied in most of the states on purchases made outside the state and brought into the state. This tax is basically levied to protect the interests of the local manufactures/traders. In some cases, the buyer/purchaser is required to pay the tax if the supplier defaults to pay the tax. This is basically done to avoid tax evasion. The tax so paid can be availed as credit by the buyer. Use tax is imposed on consumers of tangible personal property that is used, consumed, or stored in the state where it is consumed.

### **2. Venezuela**

VAT is applicable on services also. Self-Assessed tax or reverse charge is applicable if the service receiver receives the services from a service provider who is non-resident. In such cases, VAT on those services have to be paid by the service receiver /buyer of services. Service receiver can take credit for such taxes paid.

### **3. Mexico**

Services are taxed in Mexico under VAT, which is a federal tax. In case of import of services or sale of intangible goods, VAT has to be paid by the service receiver/buyer. The amount of tax can be used for offset/credit can be taken while paying the liability for VAT.

### **4. Nicaragua**

In Nicaragua, the requirements are different. VAT is applicable on exports also. VAT tax will be treated as a self-assessed tax if the buyer of the goods or services is not a VAT collector, i.e., registered under Nicaragua for VAT.

Self-assessed tax is applicable even in case if the supply of service is within Nicaragua or the use or enjoyment of property taxed, either supplied by a non-resident entity or individual or an individual resident, who are not VAT collectors, corresponding VAT will be self-assessed.

### **5. Panama**

Services and goods are taxed under VAT. In case of import of services or intangible goods, VAT taxes are applicable, and these taxes are to be paid by the importer, i.e., buyer.

### **6. Paraguay**

For import of services or intangible goods, VAT taxes are applicable. In these cases, VAT taxes are treated as self-assessed taxes and the buyer who is a local person is liable to pay VAT.

## 7. Peru

In the normal course of business, the supplier of taxable service is responsible for payment of VAT. This rule will not be applicable in cases where the supplier of services is a non-resident, VAT has to be self-assessed by the local consumer or user of services.

## 8. Argentina

In the normal course of business, the supplier of taxable service is responsible for payment of VAT. This rule will not be applicable in cases where the supplier of services is a non-resident, VAT has to be paid by the local recipient.

## 9. Colombia

The supplier is liable to charge and account for VAT on transactions except in case of import of services or non-tangible goods. VAT has to be paid by the buyer irrespective if he is registered or non-registered for VAT.

## 10. El Salvador

If the supplier of the non-tangible goods or services is a non-established entity (non-resident), VAT Tax has to be treated as a self-assessed and to be paid by the local taxpayer registered for VAT.

## 11. Guatemala

VAT taxes have to be paid by the local recipients in case of import of intangible goods or services as self-assessed taxes. In other cases, it has to be paid by the supplier of goods and services only.

For more information on self-assessed/reverse charge taxes in Latin American countries refer [here](#)

## 12. European Union

Reverse Charge or Self Assessed Tax is applicable in the European Union also. This is applicable in case of B2B sales between the European Union customer and non-European Union customer or e-commerce transactions.

The customer i.e. the buyer in the EU region has to pay the VAT tax on purchases made from other countries. The VAT tax will be treated as self-assessed or reverse charge tax by the customer.

In case of e-commerce transactions, which normally happen between business to business (B2B) the VAT taxes have to be paid by the customer as self-assessed taxes.

For additional information refer [refer](#)

## 13. Australia

Under Australian taxation for both indirect taxes under GST and VAT and also for direct taxes for withholding taxes reverse charge is applicable.

There is a mandatory reverse charge rule which broadly applies to suppliers of exempt services or real property (such as banks and life insurers). It requires these entities to reverse charge on the acquisition of services (and other intangibles) from offshore, where those supplies would be taxable if acquired in Australia. Where the reverse charge is applied, credit can then be claimed for any portion that is used to make taxable or GST-free supplies. This mandatory reverse charge does not apply to supplies that are 'connected with Australia' (see under Place of supply/taxation - general rule).

An optional reverse charge can also apply to services. In certain circumstances, the GST on taxable supplies made by non-residents can, with the agreement of the recipient, be reverse charged to the recipient. In simple terms, the GST on a taxable supply is payable by the recipient of the supply and not by the supplier if:

- the supplier is a non-resident;
- the supply is not made through a permanent establishment of the supplier in Australia;
- the recipient is registered for GST in Australia or required to be registered; and
- the supplier and the recipient agree that the GST on the supply is payable by the recipient.

For additional information can be accessed from [here](#)

## 14. Malaysia

If services are imported in Malaysia and consumed or used in Malaysia for business purpose, by a taxable person in Malaysia, then GST is applicable on reverse charge mechanism. Under this mechanism, the recipient of the imported services has to account for GST on the imported services as if he is providing the services himself and at the same time claim input tax accordingly. However, if the consulting company is not a taxable person, he has to account GST on the imported services incurred through GST-04

Organization for Economic Cooperation and Development (OECD) has given guidelines for levy of taxes on reverse charge basis for supply of services and intangibles cross-border transactions. It is commonly known as cross-border tax, and in India, it is known as Equalization Levy and applicable from 1<sup>st</sup> June 2016. Equalization Levy is also a reverse charge in nature and applicable under Income Tax Act.

The trade and business have to pay taxes under reverse charge in India or in other countries based on their legal framework and for this, we also need to have the proper accounting and software to implement this without any compliance issues along with requisite knowledge of the same.