



# Valuation of Non-monetary consideration under Service Tax



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The term 'service' is defined under service tax law to mean any activity for 'consideration' by one person for another. In this regard, it is important to note that section 67 of the finance act, 1994 determines consideration to include both monetary as well as non-monetary consideration. Monetary consideration is the consideration in the form of money and there are no any disputes on determination of the value for the same, however, liability of service tax on non-monetary consideration and its valuation has been a subject matter of dispute. Current article is written to understand the meaning of the term non-monetary consideration, its coverage, interpretation, practical issues and best course of action therein.



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## 'Non-monetary' consideration essentially means compensation in kind such as the following:

- Supply of goods and services in return for provision of service;
- Refraining or forbearing to do an act in return for provision of service;
- Tolerating an act or a situation in return for provision of service;
- Doing or agreeing to do an act in return for provision of service.

Statutory provision under section 67 of the finance act states that “in a case, where the provision of service is for a consideration not wholly or partly consisting of money, be such amount in money, with the addition of service tax charged, is equivalent to the consideration”.

In simple terms the above statutory provision states that, in case consideration for the service provided is received in the non-monetary form then we must check if the value in non-monetary form is ascertainable or is the same not ascertainable. If the value is ascertainable then the same shall be taken as the value for the service provided (For ex: 'X' provides chartered accountancy service to 'Y' for which 'Y' pays 100 grams of gold to 'X' as a consideration for the service provided. In such a case, even though consideration is in the non-monetary form still the same is ascertainable as the value of gold can be easily available) and therefore the said ascertained value shall be taken as consideration. However, the real practical valuation challenges arise in cases where consideration is paid in the non-monetary form and the value of the consideration is not ascertainable. For example:

a. A provides land to B for construction of residential apartments, in return, of which B provides 40% of the constructed flats to A; (commonly known as Joint Development agreements)

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b. A agrees to design B's house and in return B agrees not to object to construction of A's house in his neighborhood.

As per section 67(1)(iii), in case where the provision of service is for the consideration which is not ascertainable, then the value of taxable service shall be determined in the prescribed manner. In this regard, rule 3 of the service tax (determination of value) rules, 2006 has been prescribed which provides as follows:

a. The value of such taxable service shall be equivalent to the gross amount charged by the service provider **to provide similar service to any other person in the ordinary course of trade** and the gross amount charged is the sole consideration;

b. Where the value cannot be determined in accordance with clause (a), the service provider shall determine the equivalent money value of such consideration, which **shall, in no case be less than the cost of provision of such taxable service.**

In simple terms, the above rule states the value shall be determined as follows:

a. Value shall be the **"gross amount charged"** for providing the **"similar service"** to any other person in the ordinary course of trade; and

b. Further, the above value shall in no case be less than the cost of provision of such service.

The term 'similar service' referred above means a service of similar description provided under similar circumstances. However, the said expression has not been defined under the law. Neither there is any relevant judgment on this

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issue. There are judgments in relation to the expression 'similar goods', for instance, the supreme court in case of NAT steel Equipment pvt ltd v/s CCE, has stated that "... The expression 'similar' is a significant expression. It does not mean identical but it means corresponding to or resembling to in many respects; somewhat like; or having a general likeness. The statute does not contemplate that goods classed under the words of 'similar description' shall be in all respects the same. If it did, these words would be unnecessary..."

However, the criteria to determine to interpret the term 'similar goods' may not be justifiably used to determine incidence of 'similar services' since goods are tangible in nature and their similarity can be judged by seeing them or by comparing its characteristics etc. But services are intangible in nature which cannot be seen to compare it with other services and therefore the determination of monetary equivalent of non-monetary value remains an arguable issue in case of 'similar service'.

The stipulation of similar service being provided in ordinary course of business brings in the concept of independent persons and arm's length price, which in substance refers to the transaction between two unrelated parties. However, practical challenges do exist in determining whether or not a particular service can be considered as a 'similar service' for the purpose of valuation of any other service especially when the law does not envisage the nature or the degree of similarity to be relied upon. For example:

a. Can an opinion provided by a chartered accountant on one matter can be considered as similar to the opinion provided by the same chartered accountant on any other matter without giving due regard to the time, efforts and complexity involved in the other opinion?

b. In case of Joint Development agreements, can the price at which flats are sold to other customers be applied to the flats sold to the land owners treating the same as 'similar service' especially when they differ in the following aspects:

i. Flats of landowners and other customers differ in terms of area, location, time of booking, quality of construction, special services provided if any.

ii. Consideration charged/received from the customer also includes value of undivided portion of land, whereas the transaction with landowners does not cover any consideration towards undivided portion of land.

iii. Further value of flat sold to others customer also includes the finance cost unlike in case of flats sold to land owners.

In above cases, although it can be argued that the word 'similar' need not be interpreted as 'same' and any similarity shall suffice for valuation, but such an interpretation only invites for larger consequences as similar even in the most bleakest sense would entail department to adopt the higher values for the calculation of the service tax liability, causing undue hardship to the assessee.

As the government envisaged the practical difficulties in ascertaining the value of similar service, it provided alternate criteria to value the service on the basis of its cost. However, there is no commonly agreed formula for determining this aspect as well as to whether it would be on the basis of full costs comprising both direct and indirect costs or whether it would only extend to direct costs incurred for providing the services. This is particularly true in relation to determination to the cost of services, as opposed to determining the cost of supply of goods. However, in the view of the paper writer, full costs including direct and indirect costs must be considered for the purpose of valuation unless anything to the contrary is provided in the legislation.

Therefore, although the valuation rules have provided two alternate criteria to value a non-monetary consideration in case of unascertainable value of service, however, the existing provisions in this regard are not adequate to take care of this aspect.

**Conclusion:** In all cases where the value is not ascertainable, assessee may determine the same based on the service most akin and it is recommended to intimate the same to the department giving out the detailed calculation of value adopted and the reasons thereof in order to avoid any departmental disputes at a future date and to safeguard selves from extended period of limitation and unwarranted penalties on the grounds of suppression, collusion or misrepresentation etc. Also, adjustments can be made for any differences arising on account of difference in quality of service, timing or any other criteria.

Further, consideration can also be valued based on cost and more often than not the same shall be more favourable option provided if it can be established that the value in such circumstances cannot be ascertainable as the services provided are not similar in nature. It is vital to carve out the distinction and establish that the services are not similar in nature, once established, and then consideration can be valued based on actual costs incurred. Further, as a precautionary measure the valuation so adopted shall be supported by a cost accountants certificate.

The last course of action could be to opt for provisional assessment from the department but the same is usually less favorable option than others.

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