

Microsoft Dynamics® AX 2009

Service tax reverse charge mechanism for India

White Paper

According to Notification No 15/2012-ST dated 17.03.2012, a new reverse charge mechanism will be applicable from the date when Finance Bill, 2012 is enacted. Per the reverse charge mechanism, the recipient of the service is now liable to pay service tax either partially or fully.

This article is to explain the changes to Microsoft Dynamics AX 2009 to accommodate the reverse charge mechanism.

October 2012

<http://www.microsoft.com/dynamics/ax>

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Objectives and introduction

The Union Budget includes multiple proposed changes to service tax, in light of the Negative List of Services. An important aspect of the burden of tax liability under the reverse charge concept has also been proposed for replacement from existing provisions.

The new reverse charge mechanism will also be applicable to the following services:

- Rent-a-cab service
- Manpower power supply service
- Works contract service

Per the reverse charge mechanism, the recipient of the service is now liable to pay service tax either partially or fully.

Currently, Microsoft Dynamics AX already supports GTA (Goods Transport Agency) scenarios where the service recipient pays all the service tax to the authorities, which is a 100-percent reverse charge. This hotfix addresses scenarios where both the service recipient and the service provider need to pay service tax.

Standard scenario

The following are the business scenarios where both the service recipient and the service provider are liable to pay service tax:

- Hiring a motor vehicle designed to carry passengers:
 - With abatement
 - Without abatement
- Supply of manpower for any purpose
- Works contract service

The burden to pay service tax is on both the service recipient and the service provider. The service provider is liable to collect and pay a specified percentage of the service tax to the authorities. The service recipient is liable to pay a specified tax and invoice value to the service provider, and is entitled to claim a CENVAT credit for the service tax he or she paid, on the basis of the tax invoice received. The service recipient is also entitled to claim a further CENVAT credit for the tax that he or she paid under the reverse charge mechanism, on the basis of the challan details used to pay the tax authority.

In the following example, the service recipient should pay 25 percent of the service tax to the service provider and should pay the remaining 75 percent directly to the tax authority.

The following financial entry will appear in the books of the service provider.

Account	DR	CR
Customer Account	10,309	
Sales		10,000
Service Tax Payable (25%) (1236 × 25%)		309

The following financial entry will appear in the books of the service recipient when the invoice for the purchase of services is posted.

Account	DR	CR
Purchase Receipt Account (Services)	10,000	
Service Tax Recoverable (25%)	300	
E-Cess Recoverable (25%)	9	
Interim Service Tax Recoverable Account (75%)	900	
Interim E-Cess on Service Tax Recoverable Account (75%)	27	
Vendor		10,309
Interim Service Tax Payable Account		900
Interim E-Cess Service Tax Payable Account		27

If taxes are loaded on inventory, the following financial entry will appear in the books.

Account	DR	CR
Purchase Receipt Account (Services)	11,236	
Interim Service Tax Payable Account		900
Interim E-Cess Service Tax Payable Account		27
Vendor Account		10,309

Note: If the load on inventory (LOI) is 30 percent, it will be loaded proportionately, with 70 percent to Service Tax Recoverable and 30 percent to Purchase Receipt Account.

Payment scenarios

When a payment is made to the service provider, the following business scenarios can arise.

Scenario 1: Full payments to the service provider

(Per current law, service tax liability arises for the service recipient only after he or she makes full payment to the service provider.)

When full payment is made to the service provider, the following entry will appear in the books.

Account	DR	CR
Service Provider (Vendor)	10,000	
Bank		10,000

After posting, the entries generated at the same time to knock off the interim account for service tax payable appear as shown here.

Account	DR	CR
Interim Service Tax Payable (75%)	900	
Interim E-Cess on Service Tax Payable (75%)	27	
Service Tax Payable		900
E-Cess on Service Tax Payable		27

Scenario 2: Partial payment to the service provider

If the service recipient makes a partial payment to the service provider, he or she is liable to pay service tax in proportion to the value of the payment. In this example, the service provider receives INR 5,000 against the bill value of INR 10, 000.

Account	DR	CR
Vendor	5,000	
Bank		5,000

After posting, the entries generated at the same time to knock off the interim account for service tax payable appear as shown here (in proportion to the payment value).

Account	DR	CR
Interim Service Tax Payable (75%)	450.00	
Interim E-Cess on Service Tax Payable (75%)	13.50	
Service Tax Payable		450.00
E-Cess on Service Tax Payable		13.50

Scenario 3: Advance payment

If the service recipient makes an advance payment to the service provider, he or she is liable to pay service tax on the payment amount, as shown here.

Account	DR	CR
Service Provider (Vendor)	10,000	
Interim Service Tax Payable (75%)	900	
Interim E-Cess on Service Tax Payable (3% of Service Tax) (75)%	27	
Bank		10,000
Service Tax Payable		900
E-Cess on Service Tax Payable		27

Scenario 4: Payment of tax to the service tax authority

The following is the accounting entry at the time of payment to the government authority.

Account	DR	CR
Service Tax Payable (Authority Vendor)	900	
E-Cess on Service Tax Payable (Authority Vendor)	27	
Bank		927

After service tax is paid to the government, the service receiver can avail the paid service tax as a CENVAT credit for the discharge of excise duty or service tax liability. In a multiple-location environment, the CENVAT credit for paid service tax can be availed in a warehouse or location whose STC number is selected when the payment is made to the authorities.

When the service recipient pays service tax to the tax authorities, the entries generated to knock off the interim account for service tax recoverable appear as shown here.

Account	DR	CR
Service Tax Recoverable	900	
E-Cess on Service Tax Recoverable	27	
Interim Service Tax Recoverable		900
Interim E-Cess on Service Tax Recoverable		27

During the tax settlement process of the next period, the service tax recoverable amount should be available for settlement with the service tax or excise duty liability.

Main changes in the application

Item sales tax group form

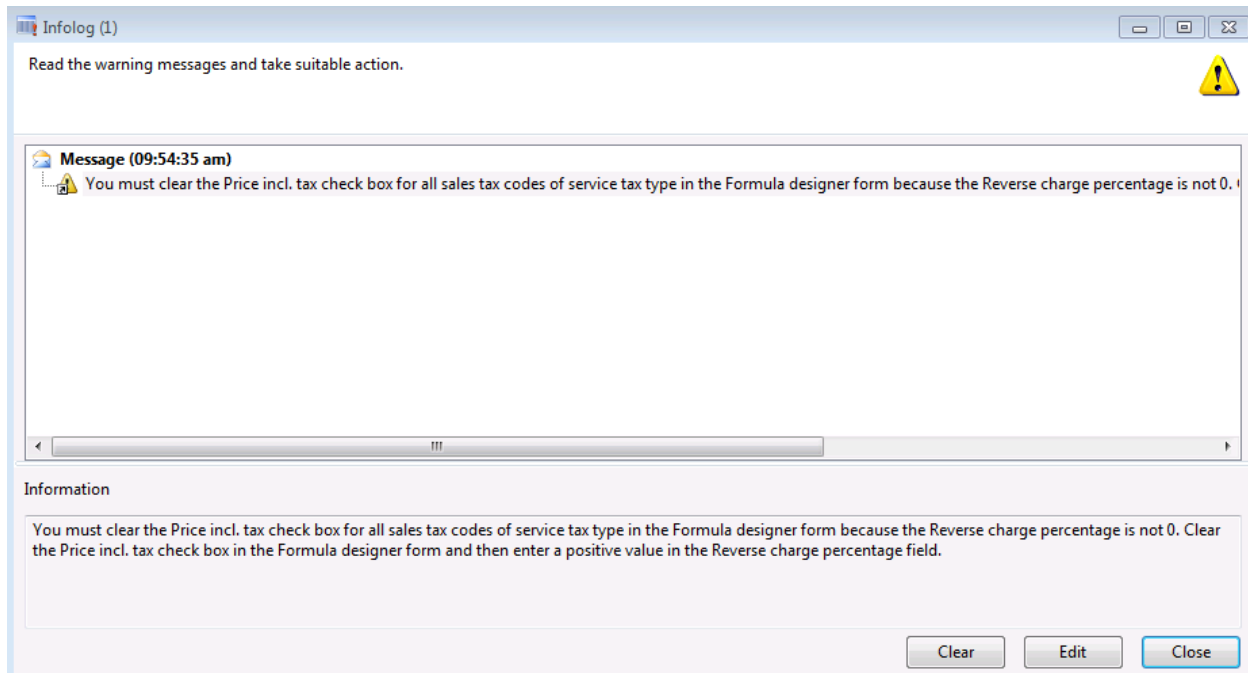
At **Main** menu > **General ledger** > **Setup** > **Item sales tax group**, the **Reverse charge percentage** field has been added to the form.

Users use this field to specify what percentage of service tax will be deducted by the service recipient and paid to the tax authority. The remaining tax will be paid to the service provider.

The field should only be enabled when the accounting basis is **Point of taxation basis**. When the accounting basis is changed to another value, the reverse charge percentage should be changed to **0**, and the field should be disabled.

The field value should be between 0 and 100. If the value is negative, it should be updated to **0** when you move the focus away from the field; likewise, if the value is more than 100, it should be updated to **100** when the field loses the focus.

For reverse charge usage, service tax should not be included in the price. Therefore, when the reverse charge percentage is not 0, if any service tax code in the formula designer has the **Price incl. tax** check box selected, you receive an error message upon saving the formula designer or item sales tax group.



Apply reverse charges to transactions

This section provides detailed descriptions of the changes in transactions. This functionality impacts vendor transactions in the following forms:

- **Accounts payable > Common forms > Purchase order details**
- **Accounts payable > Journals > Invoices > Invoice register**
- **Accounts payable > Journals > Invoices > Invoice approval journal**
- **Accounts payable > Journals > Invoices > Invoice journal**
- **Accounts payable > Journals > Payments > Payment journal**
- **Accounts payable > Journals > Promissory notes**
- **General ledger > Journals > General journal**

Compared with existing functionalities, tax calculation (total tax amount) will **not** be impacted. Therefore, load on inventory and abatement should work like the existing functionalities.

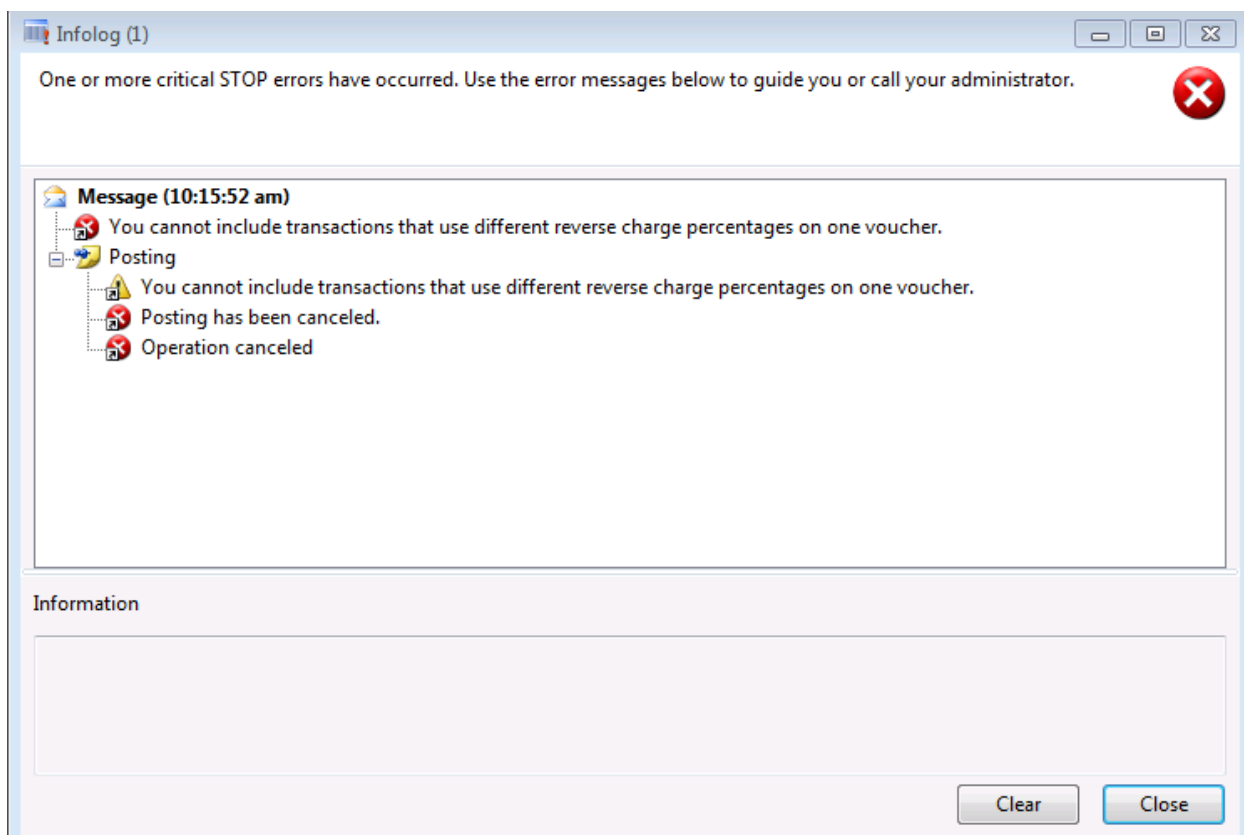
This functionality mainly involves distributing the tax amount between the tax recipient and the tax provider (the company and vendors) according to a specified reverse charge percentage, and generating corresponding accounting entries for the invoice, payment, and invoice settlement.

When the reverse charge percentage is 0, it is actually not a reverse charge, and accounting entries should be generated as for the existing point of taxation (POT).

When the reverse charge percentage is 100, the accounting entries should be the same as for existing GTA functionalities, regardless of whether the relevant vendor is a GTA vendor.

When the reverse charge percentage is between 0 and 100, the accounting entry is the weighted combination of the entries for POT and GTA.

When there are multiple lines in one voucher, the reverse charge percentages should be the same; otherwise, you receive the following error message.



An example is provided to illustrate the functionalities.

Example: Receive the manpower supply service

Company ABC receives the manpower supply service from vendor XYZ. The purchase order is created in July 2012, the invoice is issued in September 2012, and payment is made right after the invoice is received.

Per the reverse charge mechanism notification, the percentage of service tax that must be paid by XYZ is 75, and the percentage that must be paid by ABC is 25.

The following setup is done in the application.

Amount	INR 10,000
Sales tax group	SERT3 (with tax codes Service tax, E-Cess and SHE-Cess)
Item sales tax group	AV_75% (with tax codes Service tax, E-Cess and SHE-Cess) Accounting basis: Point of taxation basis Reverse charge percentage: 75%
Rate of service tax	12%
Rate of E-Cess	2%

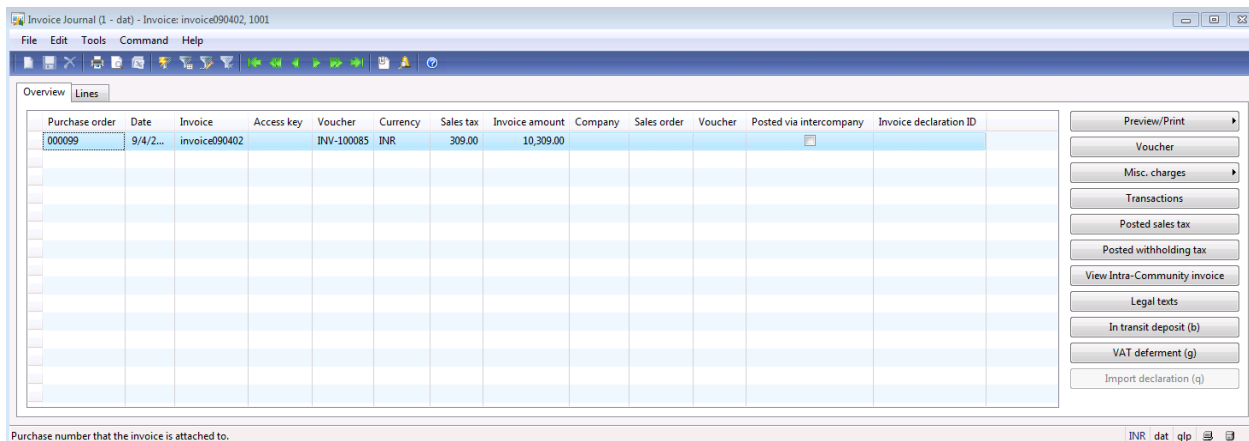
Rate of SHE-Cess	1%
Calculation base for service tax code	Line amount The Price incl. tax check box is cleared.
Calculation base for E-Cess tax code	Excl. line amount; +(Service tax) The Price incl. tax check box is cleared.
Calculation base for SHE-Cess tax code	Excl. line amount; +(Service tax) The Price incl. tax check box is cleared.

The tax amounts are 1,200 for service tax, 24 for E-Cess, and 12 for SHE-Cess, for a total of INR 1,236.

When the invoice is issued on August 12, the following voucher will be generated.

Account	DR	CR
Vendor Account		10,309.00
Service Account /PO receipt	10,000.00	
Service Tax Recoverable	300.00	
E-Cess Recoverable	6.00	
SHE-Cess Recoverable	3.00	
Interim Service Tax Recoverable	900.00	
Interim E-Cess Recoverable	18.00	
Interim SHE-Cess Recoverable	9.00	
Interim Service Tax Payable		900.00
Interim E-Cess Payable		18.00
Interim SHE-Cess Payable		9.00

The following images show the voucher.



File Edit Tools Command Help

Overview General Amount Dimension

Voucher	Date	Year closed	Ledger account	Journal	Currency	Amount currency	Amount	Amount secondary currency
INV-100085	9/4/2012	<input type="checkbox"/>	232060		INR	-9.00	9.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	232040		INR	-18.00	18.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	232020		INR	-900.00	900.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	211100		INR	-10,309.00	10,309.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	194060		INR	9.00	9.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	194050		INR	3.00	3.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	194040		INR	18.00	18.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	194030		INR	6.00	6.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	194020		INR	900.00	900.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	194010		INR	300.00	300.00	0.00
INV-100085	9/4/2012	<input type="checkbox"/>	141120		INR	10,000.00	10,000.00	0.00

Transaction text: Purchase invoice invoice0904 Posting type: Service tax

Account name: ST SHE-CCESS Interim Payable acco

Amount in secondary currency. INR dat glp

The following image shows the posted sales tax form.

Sales tax transactions (1 - dat) - Voucher: INV-100085, 9/4/2012, Apply excise: No, Date: 9/4/2012, Voucher: INV-100085

File Edit Tools Command Help

Sales tax amount in total: 309.00 Balance tax amount in total: 0.00

Investment tax: 0.00 Incentive scheme corrected amount in total: 0.00

Incentive scheme tax amount in total: 0.00 Balance corrected amount in total: 0.00

Overview General Posting Amount History

Voucher	Date	Source	Sales tax code	Sales tax direction	Voucher currency	Amount origin	Sales tax amount	Corrected a...	Sales tax charge	Reverse charge percentage
INV-100085	9/4/2012	Purchase order	ST-DL	Sales tax payable	INR	10,000.00	900.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	ST-DL	Sales tax receivable	INR	10,000.00	900.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	ST-DL	Sales tax receivable	INR	10,000.00	300.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	SHE-ST-DL	Sales tax payable	INR	1,200.00	9.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	SHE-ST-DL	Sales tax receivable	INR	1,200.00	9.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	SHE-ST-DL	Sales tax receivable	INR	1,200.00	3.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	E-ST-DL	Sales tax payable	INR	1,200.00	18.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	E-ST-DL	Sales tax receivable	INR	1,200.00	18.00	0.00	0.00	75.00
INV-100085	9/4/2012	Purchase order	E-ST-DL	Sales tax receivable	INR	1,200.00	6.00	0.00	0.00	75.00

Sales tax to be included in the cost price INR dat glp

And the following image shows the printed invoice.

Contoso Entertainment Asia-Pacific
5, Industrial Estate, Shakarpur
New Delhi-110049
New Delhi, India

Telephone: +91-11-41438683
Fax:
Giro:
Tax exempt number:
Enterprise number

Earth Televisions
789 Jones Street
Bellevue, WA 98004
United States of America

Invoice

Number: [Invoice000402](#)
Date: 9/4/2012
Page: 1 of 1
Purchase order: [000099](#)
Internal number: 10095

Payment: Net 30 days

Registration number: ND897466
TIN No.: 54397001254
ECC number: AGHPP96321<>D918
STC number:
Reverse charge percentage: 75.00

Enterprise number

Item number	Configuration	Size	Color	Description	Quantity	Unit	Unit price	Disc. pc	Discount	Amount
028				Transport Services	100.00	Pcs	100.00			10,000.00

Sales tax code	Amount origin	Quantity	Sales tax amount	Total sales tax amount
E-ST-DL	1,200.00	0.00	6.00	24.00
SHE-ST-DL	1,200.00	0.00	3.00	12.00
ST-DL	10,000.00	0.00	300.00	1,200.00

Sales balance	Total discount	Misc. charges	Sales tax	Round-off	Total
10,000.00	0.00	0.00	309.00	0.00	10,309.00 INR

cash discount granted: 200.00 INR before 9/14/2012, 50.00 INR before 10/4/2012.

When the payment is made, the following voucher is generated.

Voucher transactions (1 - dat) - Voucher: APP000087, 9/4/2012, Date: 9/4/2012, Voucher: APP000087

File Edit Tools Command Help

Overview General Amount Dimension

Voucher	Date	Year closed	Ledger account	Journal	Currency	Amount currency	Amount	Amount secondary currency
APP000087	9/4/2012	<input type="checkbox"/>	211100		INR	10,000.00	10,000.00	0.00
APP000087	9/4/2012	<input type="checkbox"/>	110152		INR	-10,000.00	10,000.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	232060		INR	9.00	9.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	232050		INR	-9.00	9.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	232040		INR	18.00	18.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	232030		INR	-18.00	18.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	232020		INR	900.00	900.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	232010		INR	-900.00	900.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	194060		INR	-3.00	3.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	194050		INR	3.00	3.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	194040		INR	-6.00	6.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	194030		INR	6.00	6.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	194020		INR	-300.00	300.00	0.00
VPY-10036	9/4/2012	<input type="checkbox"/>	194010		INR	300.00	300.00	0.00

Transaction text: Posting type: Vendor balance

Account name: Accounts Payable - US

Transaction amount in default currency. INR dat glp

Origin
Transactions
Audit trail
Posted sales tax
Posted withholding tax
Original document
Related vouchers (b)
All related vouchers (g)

The following image shows the posted sales tax form.

Sales tax transactions (1 - dat) - Voucher: VPY-10036, 9/4/2012, Apply excise: No, Date: 9/4/2012, Voucher: VPY-10036

File Edit Tools Command Help

Sales tax amount in total: 1,236.00 Investment tax: 0.00

Overview General Posting Amount History

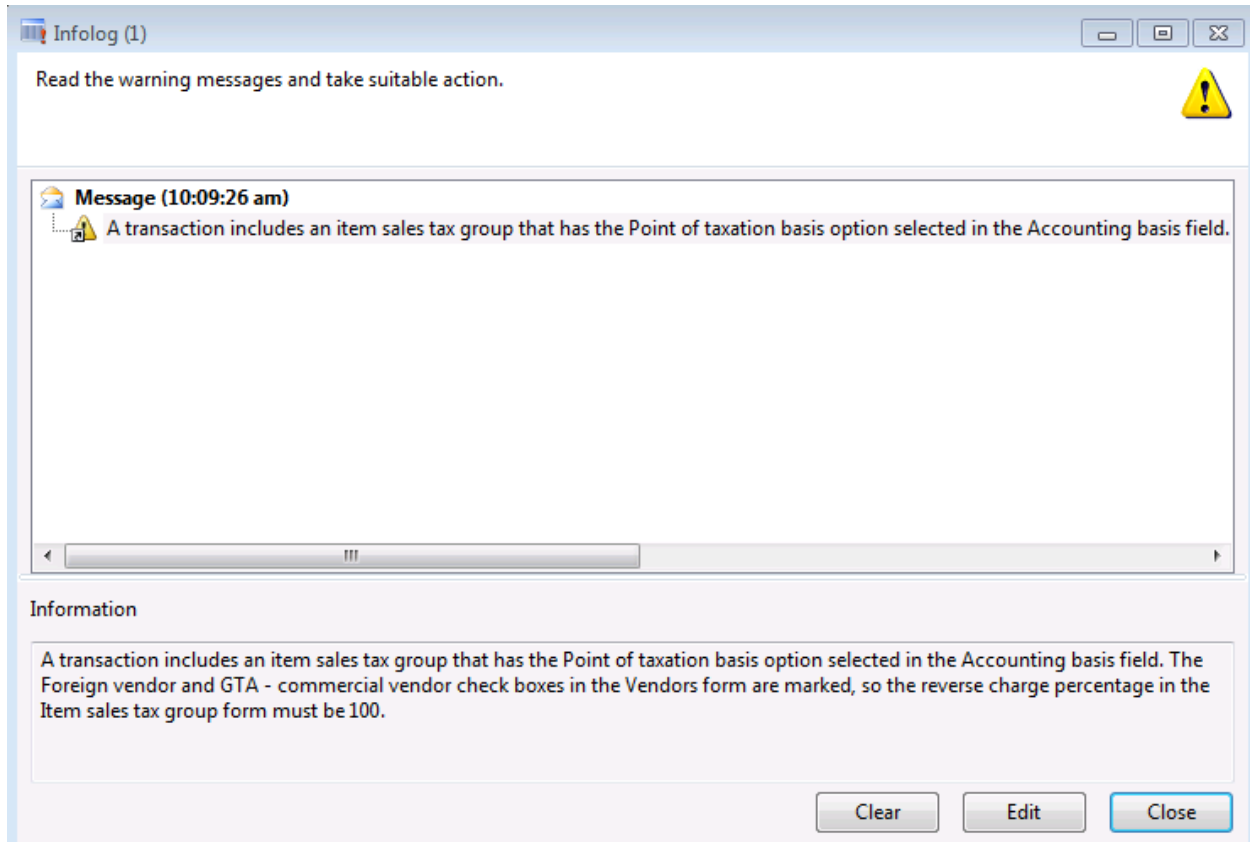
Voucher	Date	Source	Sales tax code	Sales tax direction	Voucher c...	Amount origin	Sales tax amount	Corrected a...	Sales tax charge	Reverse charge percentage
VPY-10036	9/4/2012	Voucher	SHE-ST-DL	Sales tax payable	INR	-1,200.00	-9.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	SHE-ST-DL	Sales tax payable	INR	-1,200.00	9.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	SHE-ST-DL	Sales tax receivable	INR	1,200.00	9.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	SHE-ST-DL	Sales tax receivable	INR	1,200.00	3.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	E-ST-DL	Sales tax payable	INR	-1,200.00	-18.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	E-ST-DL	Sales tax payable	INR	-1,200.00	18.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	E-ST-DL	Sales tax receivable	INR	1,200.00	18.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	E-ST-DL	Sales tax receivable	INR	1,200.00	6.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	ST-DL	Sales tax payable	INR	-10,000.00	-900.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	ST-DL	Sales tax payable	INR	-10,000.00	900.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	ST-DL	Sales tax receivable	INR	10,000.00	900.00	0.00	0.00	75.00
VPY-10036	9/4/2012	Voucher	ST-DL	Sales tax receivable	INR	10,000.00	300.00	0.00	0.00	75.00

Currency code for journal line or invoice INR dat glp

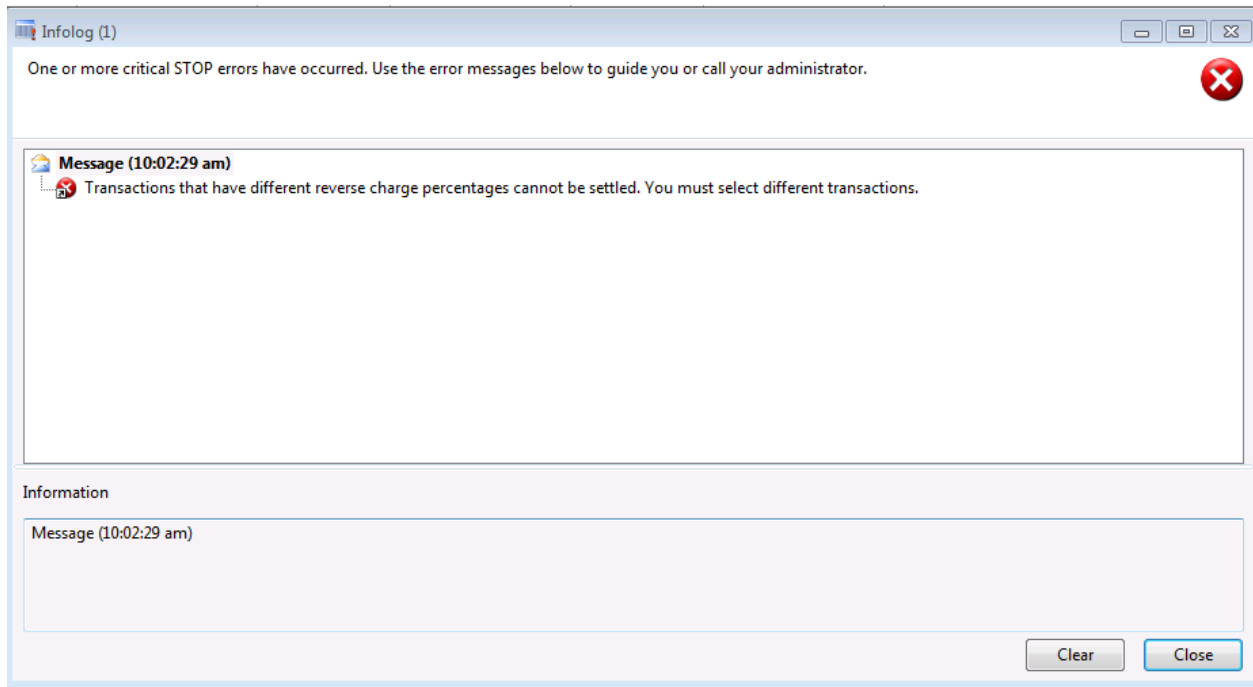
Upgrade

There is no upgrade requirement for this feature.

For GTA vendor transactions or foreign vendor transactions, users can either follow existing functionalities by using **Cash basis** as the accounting basis, or adopt the new reverse charge feature by using an item sales tax group with **Point of taxation basis** as the accounting basis and a reverse charge percentage of 100. For GTA vendors or foreign vendors, when the accounting basis is **Point of taxation basis**, the reverse charge percentage must be 100.



Note: Transactions that have different accounting bases or reverse charge percentages cannot be settled.



So, when the hotfix is applied, if there are open invoices for a GTA vendor, you still need to create according payments by using **Cash basis** as the accounting basis, and therefore you still need to settle the invoices.

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