



ANALYSIS OF PRE GST & POST GST TAXES ON WORKS CONTRACT IN CONSTRUCTION INDUSTRY

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ABSTRACTS

GST was implemented on 1 July 2017 and this change in tax system brought various changes in tax calculation in different industries. The current paper focuses on Taxes on Works Contract in construction industry where services and transfer of goods are included in one single transaction under GST regime. Earlier the tax calculation was made on both VAT and Service Tax on certain proportion of amount. The Tax calculation process was quite cumbersome, time consuming and also full of loop-holes as there was no proper method of segregating the value of services and value of goods accurately. But, after implementation of GST, the tax calculation on Works contract is simplified because one composite entry has to be made with single tax rate of 12% (or as applicable). The study has been conducted on live project of Noida, Uttar Pradesh.

Keywords: GST, Works Contract Tax, Sub – Contract, VAT, Service Tax

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1. INTRODUCTION

Ministry of Finance rolled out GST regime on 01 July 2017 and this change in taxation system turned the calculations of business entities upside down as the organizations were expecting a kind of delay in implementation of GST. Most interesting fact is that, along with firms, the government officials themselves were not prepared enough and there was a need of an entirely a new syllabus and training required to deal with the situation arise under GST regime, and to bring both entity at a common platform. According to Madrecha (2017), the

actual problem was faced by the real estate developers and construction organizations as they were having no information to manage the chorus financial activities such as payment to contractors, and taxes on works contract. The new taxation system was not equipped enough to deal with such challenges and also the users were not having such great level of understanding of the new taxation. With time, things related GST regime has been settled down under different accounting application system and the organizations have also digested up to certain level. The overall analysis of situation shows that, GST application system and its related accounting was not abnormal at any level but the actual problem arose because of lack of preparedness from both the sides, i.e. government officials related to GST and the accountants of organizations.

According to Vishwanathan (2019), the GST is implemented in order to simplify the different tax processes such as VAT, Service Tax etc. The GST implementation activity brought a drastic change in accounting concept of Works Contracts and this change could be better explained with help of tax calculation before and after implementation of GST regime. The Works Contract is actually an agreement which involve of providing services and also transfer of goods. In construction industry, the builders outsource a number of works under work contract system such as construction of building, fabrication work, electrification and interior work etc.

2. WORK CONTRACT UNDER PRE – GST REGIME

Under pre-GST regime, the work contract was managed under two different taxation process which includes Supply of Goods treated under VAT and Supply of Services treated under service tax. The Work Contract activity was treated under different taxation law and this inclusion of different taxation system was making confusion in terms of treatment of taxability and the contractors themselves were having sometimes confusion related to percentage applicability of tax under work contract.

3. WORK CONTRACT UNDER POST – GST REGIME

The implementation of GST made the entire process more simplified and now required clarification has been issued to eliminate the uncertainty of the taxation legislature. Now, the application of GST has eliminated all the confusion regarding the treatment to the taxation as now the entire contract will be treated as supply of services under GST. In GST regime the works contract is restricted to immovable property. There must be supply of both goods and services. Works contract in GST is supply of services under composite supply.

4. PURPOSE OF THE STUDY

In this study, the focus is solely on analysis of Taxes Works Contract in Pre-GST and Post-GST tax regime in construction industry. GST has been formed after clubbing of different taxation processes which include of VAT and service tax as the same was charged under works contract system. The manufactured material used in works contract is also passed through one additional tax of Excise Duty. However, the implementation of GST in Works Contract has actually simplified the complex taxation process and now the accounting has also become sorted. The current research has been conducted with aim of analyzing the complexity incalculation of taxes in Works Contract agreement in construction industry. The study is made by showing two different calculations in Pre – GST regime and subsequent Tax on Post– GST regime in Works Contract. There was difference in calculation of value of service tax in VAT and service tax rules. The study will help to discover that whether the tax amount paid is lower or higher as compared to previous tax rates and also to know the complexity involved in calculation of Taxes in Works Contracts in Pre GST regime and simplicity in GST. In this study, the subject industry, i.e. construction industry has been

chosen from Uttar Pradesh because of which the previous tax calculation will be made on basis of UPVAT and Service Tax.

5. OBJECTIVES OF THE STUDY

The objectives of the study have been shown below:

- To ascertain the difference between the tax amount to be paid on Work Contract in construction industry Pre – GST and Post – GST.
- To identify the complexity of tax to be calculated on Work Contract before GST and simplicity after implementation of GST.

6. LITERATURE REVIEW

Shinde (2019) defined the works contract under GST regime as any contract in relation to an immovable property where services are provided along with transfer of Goods. The researcher state that, the GST has been developed after elimination of three taxes, i.e. VAT, Service Tax and Central excise. The works contract tax is applicable for immovable property only and separate work account has to be created for each sub-contractor. Shinde (2019) mentioned that there is no abatement is applicable in case of works contract and the time of supply of contractual service in normal cases should be ‘Date of issue of invoice / Date of provision of service / Date of receipt of payment’. There are usually two GST rates are applicable in case of works contract tax, i.e. GST 18% and GST 12%. In the clause 2(107) of the draft Model GST law of June 2016 Movable and Immovable property both were included. To make it clear and specific in revised draft of Model GST law in November 2016 clause 2 (110) the word movable was deleted.

Piyush (2019) defines, the concept of immovable property as such Degree of permanency of the attachment to the earth, intent of the use of the goods /property is essentially of immovable nature, non-detachable without substantial loss and or lost of identity after removal. Sudipta, Abhishek and Rishabh (2019) stated that degree and the intendment and also object or intention behind the attachment to be seen to determine the immovable property. Piyush (2019) state that, the GST concept is not entertaining the aspect of nature of expenditure in terms of ‘Capital’ or ‘Revenue’. If the location of supplier, recipient and immovable property is in three different state then place of supply will be location of immovable property. If the supplier and recipient are in India and location of property is outside India then place of supply will be location of recipient. In the Works Contract Service, the Input tax credit could only be availed if works contract service is further supplied in same line of business.

The study of Mishra (2019) has specifically focused his study with respect to determining the ‘Location of the Supplier of Services’. The author mentions that, the supplier is supposed to get the firm registered with GST after attaining the stipulated limit of aggregate turnover. As far as supply of product and services is concerned then it has to be ensured that the organization must be registered with GST of principle place. He has stated that a taxable person providing the works contract service should take registration from where he is providing services. He further stated that ‘destination’ is not relevant for registration. However, this does not exactly fit as per act. This may result in loss of tax credit. Sudipta, Abhishek and Rishabh (2019)has stated that from practical perspective the contractor should be registered in the state from where the project is executed i.e. immovable property is situated.

V. S. Datey (2019) has explained the difference between Construction Service and Works Contract service. In case of works contract a recipient approaches the contractor for construction work on land of recipient. The contract is made between recipient and contractor

and material is used by contractor. This will be Works Contract. However, if the material is supplied by recipient then it will not be works contract under GST but simply a contract of work. In construction of complex the land belongs to contractor on which structure is made. The construction is done by contractor at his own and no contract is with recipient. However, in case the land is provided by some society and work is awarded to contractor for construction of premises then it is works contract.

Krishnan (2019) provided the information regarding Input Tax Credit (ITC), Tax Deducted at Source (TDS) and its applicability in case of GST under Works Contract. The author is duly mentioning that works contract is applicable only in case of immovable property and this law has been implemented in order to eliminate the process of segregating the good and service in contract. The author further mention that ITC cannot be availed by the contractor in case of immovable property until output is also works contract service. The concept of TDS was not applicable earlier but during 2018 the concept of TDS has also been introduced and now the uniform rate of TDS is 1% throughout the contract value. Manojit (2019) defines works contract as where there is transfer of goods with supply of services for contract related to immovable property. The author also supports the statement of Shinde (2019) by stating that, earlier works contract tax included of three different taxation categories, i.e. VAT, Service Tax and Central excise. The work contractor is supposed to obtain registration at any one state in case the aggregate turnover exceeds 20 lakhs and the works contractor can also apply for registration in different states. Manojit (2019) further state that, composite scheme and abatement are not available under GST regime. The works contract rate 12% and 18% are applicable in case of separate set of construction and contract activity.

7. METHODOLOGY

“Historical research’ methodology will be used in this study and one of the prominent real estate company of Noida, Uttar Pradesh will be used for the study. Prior permission from project manager has already been obtained to use the data but the name of project could not be revealed because of privacy issue. The construction project is taken for study where the works contract tax before and after implementation of GST is applicable. Earlier, when the taxes on works contract was calculated under VAT and service tax then at that time, 70% of the cost was allocated to goods and rest 30% of the cost was allocated to services under UPVAT when the complete details of materials and services was not available. Further, when service tax was to be paid then as per service tax rules 40% service tax to be paid when complete details of materials and services not available. Now, the GST is calculated on the entire amount with uniform rate of GST. GST was implemented by Government of India on 1 July 2017 and before that, a separate set of complex calculation was supposed to made while making payment for VAT and Service tax under prior tax regime. The calculation of taxes on works contract has been made by obtaining the first hand data from the project site after requesting project manager of a prominent construction company. The calculation includes of quantity and cost of the material along with service expenses.

8. ASSUMPTIONS & LIMITATIONS OF STUDY

The construction phase of a real estate project takes a time duration of 2 to 3 years and during this entire period, different sub- contractors may be engaged by construction company to carry out the work, such as electrical contractor, plumbing contractor, painting and white washing contractor, sanitary contractor etc. The sub-contracting may be for supply of material or for job work. This will have impact on tax calculation. For example, in case of painting and whitewashing contract, the paint and whitewash used have been treated as goods which was considered as 70% of the entire contract and charged under VAT whereas 30% of the cost

belongs to service charge of painting job and was charged under service tax. There will be difference of tax impact if the entire work is done by the contractor by purchasing the material and employing the labour and on other hand the complete work of white washing is subcontracted. But now, after implementation of GST, the entire 100% of the amount is charged under GST at flat tax rate. The tax rates may be changed due to some political interference under special circumstances or requirements in a particular state. The prices of raw material may change over a period of time which will have impact on tax also. In this study, it is assumed that, there is no significant impact of change due to any reason.

9. ANALYSIS

The definition of “Works Contract” under service tax is as under:

“Works Contract “means a contract where in transfer of property in goods involved in the execution of such contract is leviable to tax as sale of goods and such contract if for the purpose of carrying out construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, alternation of any movable or immovable property or for carrying out any other similar activity or a part thereof in relation to such property”.

The definition of works contract as per UP VAT Act is as under:

“Works Contract includes any agreement for carrying out, for cash, deferred payment or other valuable consideration, the building, construction, manufacture, processing, fabrication, erection, installation, fitting out, improvement, modification, repair or commissioning of any movable or immovable property.”

Central GST defined the work contract as under:

“**Works Contract**” means a contract for building, construction, fabrication, completion, erection, installation, fitting out, improvement, modification, repair, maintenance, renovation, alternation or commissioning of any immovable property wherein transfer of property in goods

(whether as goods or in some other form) is involved in the execution of such contract

There are two different methods employed to calculate the value of service tax and VAT as per earlier tax regime. In service tax as well as in VAT, both the method is adopted. In the first method the value of goods and services used in the carrying out the project would be ascertained as per actual cost of goods and services whereas in second method, the value of goods and services could not be ascertained specifically, so the entire calculation is made with help of percentage value as provided in respective acts.

9.1. Actual Calculation Scenario

In this study, a live project of Uttar Pradesh has been taken. The data has been collected from the project manager and some of the figures and values of the BOQ has been changed in order to maintain the secrecy of project. The real estate project requires approximately 1300 line of items (BOQ) items. In order to sort out the calculation, those 1300 items have been group under headings of 50 different material segment. The rate as per VAT has been separately identified which is quite complicated and time-consuming process. However, after implementing such a cumbersome method of value calculation, the cost of material could not be ascertained with 100% accuracy. The item wise detail has been shown in appendix.

Calculation Method 1

Table 1 Summary of Material Purchased and VAT Payable/Paid

The method is implemented when accurate value of labour, service, goods and profit could be ascertained

SL.	DESCRIPTION	SALES VALUE (original BOQ value)	VAT
A	B	C	D
1	Total of items with 0% rate	5463409	0
2	Total of items with 5% rate	166564220	7931630
3	Total of items with 14.5% rate	157293967	19919323
4	Total of items with 16.5% rate	32584605	4614987
5	TOTAL->	361906201	32465940

Figures from Appendix Table

Table 2 Calculation of TAX as per Method 1

As per UP VAT rules WCT was required to be deducted and deposited from contractor bills. calculation is as under:

SL.	Description	Value (Rs.)
A	B	C
1	Total BOQ value (Gross receivable)	656734693
2	WCT to be deducted @ 4%	26269388
3	Total VAT to be paid	32465940
4	Balance short tax to be deposited (Row 3-2)	6196552
5	Service Tax to be paid	29016107
6	ED to be paid	31851321
7	Additional TAX to be paid	8976748
8	Total Tax (A3+A5+A6+A7)-->	102310116

Figures from Appendix Table

Calculation Method 2

The method is implemented when accurate value of labour, service, goods and profit could not be ascertained. In such scenario, UP VAT enables the organization to charge 30% on the value as cost of labour and profit in construction project and balance 70% as value of goods and profit thereon.

Table 3 Cost of Project and Value of Goods

SL.	DESCRIPTION	AMOUNT (Rs.)
A	B	B
1	Cost of project/Total Receivable amount	656734693
2	Value of goods (70%)	459714285
3	Total purchase value of Goods	361906201
	Figures from Appendix Table	
Value addition= Gross receivable of Goods (A2)/Total Purchase Value of Goods (A3) - >1.270258105		

Table 4 Summary of Purchase of Material and value addition

SL.	Description	Purchase value of Goods	Vaue of goods after adding Factor 1.270258105	Vat %	VAT
A	B	C	D	E	F
1	Total of items with 0% rate	5463409	6939940	0	0
2	Total of items with 5% rate	166564220	211579550	5	961725
3	Total of items with 14.5% rate	157293967	199803937	14.5	28971571
4	Total of items with 16.5% rate	32584605	41390858	16.5	6829492
	Total-->	361906201	459714285		36762788
Figures from Appendix Table					
As per service tax valuation rules when details are not available then it is 40% of Gross receivables					

Table 5 Calculation of Tax as per Method 2

SL.	DESCRIPTION	AMOUNT (Rs.)
A	B	C
1	Cost of project/Total Receivables	656734693
2	40% of services	262693877
3	Service Tax @15%	39404082
4	VAT (##)	36762788
5	ED to be paid	31851321
	Total Tax (A3+A4+A5) -->	108018191
Figures from Appendix table and (##) Table 4 above		
Remark: Value addition has been done by factor 1.27. So value addition of tax is already included		

The above two different method of calculation show that, the entire tax calculation is quite cumbersome and also it is almost impossible to determine the exact value and quantity of the items. In pre-GST method of tax calculation, the chances of mistake and misrepresentation is quite possible but now the GST has simplified the entire calculation.

Table 6 Calculation of Tax, Considering impact of Method 1 & Method 2 (Under GST Regime)

SL.	DESCRIPTION	AMOUNT (Rs.) Method 1	AMOUNT (Rs.) Method 2
A	B	C	D
1	Toalreceivable from client	656734693	656734693
2	Less: Total Tax (Pre-GST)	102310116	108018191
3	Receivable without taxes (A1-A2)	554424577	548716502
4	GST @ 12%	66530949	65845980.3
5	Total Project Cost Post GST (A3 + A4)	620955526	614562483
6	Percentage (%) reduction in project cost	5.45	6.42

Figures from Table 2 and Table 5 above

Table 7Summary of Taxes (Pre and Post GST Regime)

SL .		Total Tax PRE GST	Total Tax Post GST	Total Cost Pre GST	Total Cost Post GST	Percentage reduction Post GST
1	Method 1	102310116	66530949	656734693	620955526	5.45
2	Method 2	108018191	65845980	656734693	614562483	6.42

Figures from Table 2 and Table 5 above

The above working shows that the Post GST total tax is less and calculation method is also easy.

10. DIFFERENCE BETWEEN PRE – GST & POST – GST CALCULATION OF WCT

Particulars	Pre - GST	Post – GST
Scope	Works contract includes both movable and non – movable property.	The works contract is applicable only in case of immovable property.
Complexity	The process of calculation of taxation was quite cumbersome and time consuming. In works contract act, there is separate tax calculation for both service tax and VAT by segregating the values on basis of service charge and goods purchased and transferred with contract.	A single and composite calculation of taxes on Works Contract is made.
Other Material Inclusion	The consumables are not taxable under VAT law but is charged under service tax law. Free of cost materials are not charged under any tax regime.	Consumables are charged under GST single tax value. Free of cost materials are not charged under any tax regime.
Tax Deduction at Source	TDS is applicable under VAT regime as in UP, the TDS is deducted at the rate of 4%. No TDS is applicable in case of service tax	TDS is applicable from 01.10.2018.

11. CONCLUSIONS

GST is one of the prominent and historical tax provisions implemented on 01 July 2017 in India. The change in tax system affected the entire business of country as the entrepreneurs faced quite a difficult time while coping with change. GST implementation acted as boon and bane for different industries. In most of the industries it acted as boon due to tax reduction only in few cases the tax is increased. However, in all the cases industries overcame the problem of cumbersome tax issue. The current paper focuses on Taxes on Works Contract in construction industry. Works contract system refers to the situation where concept of supply of goods and service charge included in one single transaction. The study is conducted on a live real estate project of Noida but the name could not be revealed because of privacy concern. The study concluded that, under Pre – GST regime, there was separate calculation for VAT and Service Tax where value of goods and service charges are ascertained separately. The tax calculation was quite cumbersome and time consuming but under GST regime, the tax calculation is quite sorted and simplified. In post GST regime, the taxes in Works Contract work is less than the Pre GST regime.

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APPENDIX TABLE

S No.	Particulars	Original BOQ Value	Vat Rate	ED Rate	Service Tax Rate	ED	VAT	Service Tax	VAT paid on value addition (app 15%)
A	B	C	D	E	F	G	H	I	J
						$\frac{(C-H)}{(100+E)*E}$	$C/(100+D)*D$	$C/(100+F)*F$	$H*15\%$
1	Sand 0%	5165089	0	0	0	0	0.00		0
2	Ready Mix Concrete 0%	0	0	2		0	0.00		0.00
3	Other Materials 0%	295066	0	12.5		32785	0.00		0.00
4	Wood 0%	3254	0	0		0	0.00		0.00
(A)	TOTAL (A)-->	5463409				32785	0.00		0.00
5	Sand 5%	11949129	5	0		0	569006		85351
6	Stone 5%	838583	5	0		0	39933		5990
7	Stone Aggregate 5%	17614002	5	0		0	838762		125814
8	TMT Bars 5%	74712412	5	12.5		7906075	3557734		533660
9	Iron & Steel 5%	1907931	5	12.5		201897	90854		13628
10	Flooring Material 5%	725339	5	12.5		76755	34540		5181
11	Brick Aggregate 5%	10600	5	0		0	505		76
12	Fly Ash Bricks 5%	8253192	5	0		0	393009		58951
13	Glass Material 5%	3264972	5	12.5		345500	155475		23321
14	Hardware 5%	755679	5	12.5		79966	35985		5398
15	Finishing Material 5%	910379	5	12.5		96336	43351		6503
16	Diesel Generator 5%	2145672	5	12.5		227055	102175		15326
17	Other Materials 5%	12817663	5	12.5		1356366	610365		91555
18	Plumbing Material 5%	4750260	5	12.5		502673	226203		33930

19	Electric Material 5%	25908407	5	12.5		2741630	1233734		185060
(B)	TOTAL (B) -->	166564220				13534255	7931630		1189744
20	Stone 14.5%	423350	14.5	0		0	53612		8042
21	Iron & Steel 14.5%	1660594	14.5	12.5		161145	210294		31544
22	Glass Material 14.5%	6751444	14.5	12.5		655162	854986		128248
23	Hardware 14.5%	624131	14.5	12.5		60566	79038		11856
24	Lifts 14.5%	5829821	14.5	12.5		565727	738274		110741
25	Other Materials 14.5%	39695515	14.5	12.5		3852064	5026943		754041
26	Paint Materials 14.5%	1557597	14.5	12.5		151150	197250		29588
27	Panels 14.5%	280077	14.5	12.5		27179	35468		5320
28	Plumbing Material 14.5%	2569319	14.5	12.5		249327	325372		48806
29	Electric Material 14.5%	64104522	14.5	12.5		6220720	8118040		1217706
30	Wood 14.5%	459154	14.5	0		0	58146		8722
31	Flooring Material 14.5%	12597867	14.5	12.5		1222500	1595363		239304
32	Fly Ash 14.5%	17162	14.5	0		0	2173		326
33	Finishing Material 14.5%	5411607	14.5	12.5		525144	685313		102797
34	Diesel Generator 14.5%	7099650	14.5	12.5		688952	899082		134862
35	Sundries	8212156	14.5	12.5		796910	1039967		155995
(C)	TOTAL (C)-->	157293967				15176546	19919323		2987899
36	Cement 16.5%	32442222	16.5	12.5		3094156	4594821		689223
37	Other Materials 16.5%	142383	16.5	12.5		13580	20166		3025
(D)	TOTAL (D) -->	32584605				3107735	4614987		692248
(E)	TOTAL (A+B+C+D)-->	361906201				31851321	32465940		4869891
38	Machinery	11152214			15			1454637	218195
39	Labour 0%	134549172			15.0			17549892	2632484
40	Labour Electric 0%	64204647			15.0			8374519	1256178
41	Overheads	45291979			3.75			1637059	
(F)	TOTAL (F)-->	255198011						29016107	4106857
(G)	Contractors Profit (G)-->	39630481							
(H)	TOTAL- H (E+F+G) -->	656734693				31851321	32465940	29016107	8976748
	<u>Remark</u>								
1. On sundries VAT is charged @ 14.5%.									
2. Some grouping for rate of taxation is made to make it simpler and for the data for confidentiality .									
3. Original BOQ is changed with some % for confidentiality of data with no impact on outcome.									

Analysis of Pre Gst& Post Gst Taxes on Works Contract in Construction Industry

4. Value addition on which VAT is applicable is taken as 15%.

5. Value addition VAT and Service Tax is taken. No value addition of service tax on overhead.

6. Service tax on overheads taken only on 25% as other misc expenses like interest etc not taken.
