

4.1 INTRODUCTION & BRIEF LEGISLATIVE HISTORY

The powers conferred on the Central Government under clause (xvtaa) and clause (xvta) of section 37(2) of the Central Excise Act, 1944 lead to introduction of Central Value Added Tax (CENVAT). Section 37(2) (xvta) empowers the Central Government to make rules to provide for the credit of duty paid or deemed to have been paid on the goods used in or in relation to manufacture of excisable goods. Section 37(2) (xvtaa) empowers Central Government to make rules to provide for credit of service tax leviable under Chapter V of the Finance Act, 1994, paid or payable on taxable services used in, or in relation to, the manufacture of excisable goods.

Cenvat was initially introduced as Modvat. With effect from 1.3.1986 manufacturers were entitled to avail credit of duty paid on inputs used in or in relation to manufacture of the end products.

The scheme ensured that duty paid on input stage is offset against the duty payable at the final product stage. The object was to prevent cascading effect of duty on the final products. Later, this scheme was extended to capital goods to be effective from 1-3-94. In the year 1997, the entire rules were recasted but distinct rules were maintained for inputs and capital goods.

Over the years, disputes between the department and assesseees on the interpretation of Modvat rules and procedures plagued the system. With the intention to put an end to this situation, Budget 2000 unified the rules for capital goods and inputs into one set of rules (Rules starting from Rule 57AA to 57AK) which were simple and transparent. Subsequently, Cenvat Credit Rules, 2001 were introduced vide Notification No. 31/2001 dated 21st June 2001 which were similar to the old rules 57AA to 57AK of Central Excise Rules, 1944. These rules were again superseded by Cenvat Credit Rules, 2002 which were notified vide notification No.5/2002 dated 1.3.2002.

4.2 CENVAT CREDIT RULES, 2004

On 10.09.2004 yet another new set of rules, Cenvat Credit Rules, 2004 have been released to replace the existing Cenvat Credit Rules, 2002 and Service Tax Credit Rules, 2002.

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These rules provide for integration of manufacturing sector and service sector, for the purpose of setting off the duty incidence.

The new Cenvat Credit Rules 2004 are a follow up of the Union Finance Minister Mr P. Chidambaram's assurances in the Parliament for taking steps to integrate the tax on goods and services. The new rules mark a beginning towards a fully integrated 'Goods and Service tax' recommended by the Kelkar committee in July 2004. In other words, duties of excise paid on inputs/capital goods and service tax paid on input services can be adjusted against a manufacturer's excise duty liability or a service provider's service tax liability. Excise duty and service tax shall continue to be separate levies.

The Cenvat Credit Rules, 2004 extend to the whole of India. However, the provisions of these rules in relation to availment and utilization of credit of service tax shall not apply to the State of Jammu and Kashmir as service tax law is not applicable to Jammu & Kashmir. The rules cover all the three categories, namely manufacturers, service providers and manufacturers-cum-service providers.

4.3 RULE 2 - DEFINITIONS

The Cenvat rules have to be interpreted progressively to ensure that the purpose of the scheme is preserved. Therefore, the Rules are to be read liberally and not literally.

4.3.1 Capital goods : Rule 2(a) defines capital goods to mean

(A) the following goods, namely:-

(i) all goods falling under Chapter 82, Chapter 84, Chapter 85, Chapter 90, heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804 of the First Schedule to the Excise Tariff Act;

(ii) pollution control equipment;

(iii) components, spares and accessories of the goods specified at (i) and (ii);

(iv) moulds and dies, jigs and fixtures;

(v) refractories and refractory materials;

(vi) tubes and pipes and fittings thereof; and

(vii) storage tank,

used-

(1) in the factory of the manufacturer of the final products, but does not include any equipment or appliance used in an office; or

(2) for providing output service;

(B) motor vehicle registered in the name of provider of output service for providing taxable service as specified in sub-clauses (f), (n), (o), (zr), (zzp), (zzt) and (zzw) of clause (105) of section 65 of the Finance Act.

4.3.2 Exempted Goods: Rule 2(d) defines "exempted goods" as goods which are exempt from the whole of the duty of excise leviable thereon and includes goods which are chargeable to "Nil" rate of duty.

4.3.3 Exempted Services: Rule 2(e) defines exempted services as taxable services which are exempt from the whole of the service tax leviable thereon, and includes services on which no service tax is leviable under section 66 of the Finance Act.

4.3.4 Final Products : Rule 2(h) defines "final products" as excisable goods manufactured or produced from input, or using input service. Excisable goods are defined in section 2(d) of the Act to mean "goods which are specified in the Tariff as being subject to a duty of excise. Therefore, this term is wide enough to cover all products, whether final or intermediate, which are manufactured by the assessee by a manufacturing process. This may also include the goods which are exempted by way of notification.

4.3.5 First Stage Dealer: Rule 2(ij) means a dealer who purchases the goods directly from-

- (i) the manufacturer under the cover of an invoice issued in terms of the provision of Central Excise Rules, 2002 or from the depot of the said manufacturer, or from premises of the consignment agent of the said manufacturer or from any other premises from where the goods are sold by or on behalf of the said manufacturer, under cover of an invoice; or
- (ii) an importer or from the depot of an importer or from the premises of the consignment agent of the importer, under cover of an invoice.

4.3.6 Inputs : Rule 2(k) defines input as

(i) all goods, except light diesel oil, high speed diesel oil and motor spirit, commonly known as petrol, used in or in relation to the manufacture of final products whether directly or indirectly and whether contained in the final product or not and includes lubricating oils, greases, cutting oils, coolants, accessories of the final products cleared along with the final product, goods used as paint, or as packing material, or as fuel, or for generation of electricity or steam used in or in relation to manufacture of final products or for any other purpose, within the factory of production;

(ii) all goods, except light diesel oil, high speed diesel oil, motor spirit, commonly known as petrol and motor vehicles, used for providing any output service;

Explanation 1.- The light diesel oil, high speed diesel oil or motor spirit, commonly known as petrol, shall not be treated as an input for any purpose whatsoever.

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Explanation 2.- Input include goods used in the manufacture of capital goods which are further used in the factory of the manufacturer *but shall not include cement, angles, channels, centrally twisted deform bar (CTD) or thermo mechanically treated bar (TMT) and other items used for construction of factory shed, building or laying of foundation or making of structures for support of capital goods..*

For the purpose of better understanding, if split, the above definition it comes out as follows:

Input means

- a. All goods (except HSD, LDO and Petrol) used in or in relation to the manufacture of final products directly or indirectly and whether contained in the final product or not; and
- b. Includes -
 - i. lubricating oils;
 - ii. greases,
 - iii. cutting oils,
 - iv. coolants,
 - v. accessories of the final products cleared along with the final products,
 - vi goods used
 - as paints
 - as packing material,
 - as fuel,
 - for generation of electricity or steam used for manufacture of final products
 - or for any other purpose, within the factory of production.
- c. All goods, except light diesel oil, high speed diesel oil, motor spirit, commonly known as petrol and motor vehicles, used for providing any output service.

It would be worthwhile to examine the scope of the term “input”. The definition of the term is given in two parts. The first part gives the wide definition covering all the goods used in or in relation to manufacture. The use may be direct or indirect. Also it is not relevant whether the inputs form an identifiable part in the finished product on which duty has to be paid. The second part of the definition gives the list of various examples of inputs to be included in the definition of inputs. The said examples are basically given to clarify the issues which were persisting in the earlier Modvat scheme. In the Modvat scheme there was an issue as to eligibility of the Modvat on goods used as paints, fuel, packing materials, used for generation of electricity and also regarding parts and accessories just fitted in the final product or given along with the final product.

Further, if we analyse, inputs mean anything that is put into the stream of manufacture. Manufacture in excise is an inclusive definition that includes incidental and ancillary processes necessary for completion of a manufactured product. The term inputs is only given an inclusive definition in the Rules and would therefore tend to have a wide meaning so as to cover raw materials, components, consumables, parts etc. but will exclude capital goods as defined in Rule 2(a). The cardinal tests would be to see whether:

- (a) the inputs are used “in or in relation to manufacture” of the goods
- (b) the inputs do not fall within the excluded category, for e.g., plant/machinery/tools, etc. which are eligible for capital goods credit.

If the above tests are satisfied, then the item would be an eligible input for the purpose of Cenvat.

The term “input” should be viewed in the light of the fact that the Cenvat scheme is a beneficial legislation and should be given as wide a meaning as possible.

A combined reading of definition of capital goods and inputs shows that capital goods which are used as component parts in the manufacture of final products are eligible for Cenvat credit as inputs. The Tribunal in case of *Digital Equipment's case* - 1996 (86) E.L.T. 127 has held that small computers would be considered as a component part of large computers thereby, making them eligible for MODVAT credit as an input.

The large bench of the Tribunal in *Union Carbide India Ltd v. CCE* - 1996 (86) E.L.T. 613 held that parts of machines are also eligible for MODVAT credit as inputs. The decision was rendered in respect of a case prior to introduction of MODVAT on capital goods under MODVAT Scheme. However, this goes to show the wide scope given to the term inputs.

Considering the above definition of inputs, we need to examine the definition in detail:

Inputs used as fuel

With effect from 1-3-1994, inputs used as fuel were made specifically eligible for MODVAT credit. Fuel is basically raw material for fire. Even prior to this amendment, there were several Tribunal decisions holding that oxygen and acetylene gas were eligible inputs when used as fuel. Explanation to Rule 2(g) excludes HSD, LDO and petrol from the scope of inputs irrespective of the use to which they are put. It is also unfortunate to note that clause 108 of the Finance Act, 2000 disallowed HSD as an input with retrospective effect from 16-3-1995 and recover all duties which have been taken from that date. There is no basis for this bias towards the fuel by the Legislature which is unfortunate.

Inputs used for generation of electricity or steam

This clause was introduced originally in Explanation to Rule 57A with effect from 16-3-95. In *Ballarpur Industries Ltd v. CCE* 2000 (116) E.L.T. 312, the Larger Bench of the Tribunal and in *Reliance Industries Ltd v. CCE* - 1997 (93) E.L.T. 213 (T-WZB) the Tribunal has held

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that furnace oil, light diesel oil and low sulphur heavy stock used as fuel in producing steel which in turn is used in the manufacture of final products is eligible for credit. However, now light diesel oil has been excluded from the list of inputs eligible for cenvat credit. The Tribunal has noted that this is the position even prior to 1995 when the amendment was introduced. The only condition is that the electricity or steam generated is to be used in the factory of production for any purpose. The Tribunal has held in *Rathi Alloys and Steel Ltd v. CCE - 1997 (93) E.L.T. 594 (T-NZB)* that residual fuel oil and low density oil used in generators for making electric arch furnace operational is covered by the clause "inputs used as fuel" and the later amendment including inputs used for electricity or steel is only clarificatory and therefore retrospective in effect. In the new definition of the input it is clearly spelt out that the goods used for generation of electricity or steam used for manufacture of final products or for any other purpose, within the factory of production are eligible for credit. It would be pertinent to note that steam falls within Chapter 28.51 of the Excise Tariff but electricity is not an excisable good since it is not found in the Tariff at all. This would be clear when one looks at Customs Tariff wherein electrical energy is included in Chapter 27.16 of the Tariff. Irrespective of whether they are excisable goods or not, inputs used for their generation are eligible provided they are consumed captively within the same factory. Therefore, power plants whose end product is generation of electricity would not be eligible for Cenvat credit unless they are located inside the factory of manufacture of other excisable goods.

Packing materials

Rule 2(k) includes in its definition the goods used as packing materials whereby it allows credit on packing materials. There seems to be no restriction on those packing materials which do not enter the assessable value. It would be worthwhile to look briefly at the chequered history of packing materials as regards its eligibility.

In the erstwhile Explanation to Rule 57A, packaging material was eligible for MODVAT credit. This was interpreted by the Department as including only ready to use packages and not raw materials used for manufacturing such packages. However, this controversy was set at rest by the Madras High Court in *Ponds India Ltd v. CCE 1993 (63) E.L.T. 3* wherein the High Court held that the term packaging materials means not only ready to use packages but also raw materials used to manufacture such packages. Rule 57B very specifically says packing materials and materials from which such packing materials are made are eligible inputs provided the cost of such packs is included in the value of finished product.

Accessories [2(k)]

The term accessories is defined in Oxford English Dictionary as something contributing in a subordinate degree to a general result or effect as distinguished from parts which are essential to make the commodity and on which credit is available under Rule 3. Websters Dictionary defines it as something extra or something added to help in a secondary way.

Generally, an accessory is an object that is not essential in itself but, adds to the beauty, convenience or effectiveness of something else. The amendment to include accessories as an eligible input came about with effect from 29.6.95 in the erstwhile Explanation to Rule 57A (vide notification 28/95). However, the Tribunal took a view in *BPL Sanyo Ltd v. CCE* - 1996 (82) E.L.T. 337 (T-SRB SM) that accessories have never been excluded from the scheme of MODVAT. The present Rule as it stands today is that accessories which are cleared along with the final product is eligible for Cenvat credit. Therefore, if accessories are supplied after clearance of the final products, they will not be eligible for MODVAT credit. The Supreme Court has held in *CCE v. Jay Engg. Works Ltd.* - 1989 (39) E.L.T. 169, that name plate affixed on the fan is an eligible input since they are essential for marketing the fans. This view was reiterated by the Supreme Court in *HMM Ltd v. CCE* - 1994 (74) E.L.T. 19, wherein it was held that metal screw cap put on Horlicks bottle is a component part of the finished product.

Lubricating oils, greases, cutting oils and coolants

These items are now specifically included in the definition of the inputs. With effect from 1.3.97, lubricating oils, greases, cutting oils and coolants were excluded from the scope of inputs and they were specifically held eligible under Rule 57Q pertaining to MODVAT on capital goods. But, with effect from 1.9.97, lubricating oils, greases, cutting oils and coolants had been given the benefit of both Rules 57B and 57Q. However, it must be noted that prior to 1.3.97, there were numerous judgements in which lubricating oils were held eligible for MODVAT credit as inputs. See Tribunal decision in *Pragati Paper Mills Ltd v. CCE* - 1996 (88) E.L.T. 137 (T-NZB SM) and *CCE v. Kunal Engg. Co. Ltd* - 1992 (62) E.L.T. 560 (T-SRB). Even this controversy is settled by decision of Larger Bench in *CCE v. Modi Rubber Ltd.* - 2000 (119) E.L.T. 197 (T-LB), wherein the Larger Bench held that lubricating oils and greases are eligible for Modvat.

Inputs manufactured and used within the factory of production

Though there is no express provision for such cases in Rule 3, it is implied that credit is allowable since the final product manufactured is dutiable. If an assessee manufactures certain goods that are consumed by him in the further manufacture of other end products, Rule 4 of the Central Excise Rules, 2002, deems captive consumption as amounting to removal under the Excise Rules. This concept was brought about vide notification 20/82, dated 20.2.82 with retrospective effect from 1944 in Rules 9 & 49 of CER, 1944. This amendment was upheld by the Supreme Court in *J.K. Spinning and Weaving Mills Ltd v. UOI* - 1987 (32) E.L.T. 234. Therefore, captive consumption of inputs attracts the levy of excise which can be modvated by virtue of this Rule. It would also be pertinent to note that currently Notification No. 67/95, dated 16.3.95 exempts inputs manufactured and consumed captively for production of final products on which duty is payable. The Board in its supplementary instruction dated 1-9-2001, has clarified that Cenvat credit should not be denied if the inputs are used in any intermediate product arising in the course of

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manufacture of the final product (dutyable) even if such intermediate product is exempt from payment of duty.

Paints

Paint has been specified as an input under Rule 2(k) though normally it is used only after the product is completed. Painting ensures that the final product becomes marketable and therefore, they have expressly included it as input. Thinners that are used to dilute paints are also eligible for MODVAT credit as per the decision of the Tribunal in *CCE v. Facit Asia Ltd.* - 1992 (60) E.L.T. 157 (T-SRB).

A combined reading of definition of capital goods and inputs shows that capital goods which are used as component parts in the manufacture of final products are eligible for Cenvat credit as inputs. The Tribunal in case of *Digital Equipment's* case - 1996 (86) E.L.T. 127 has held that small computers would be considered as a component part of large computers thereby, making them eligible for MODVAT credit as an input.

The large bench of the Tribunal in *Union Carbide India Ltd v. CCE* - 1996 (86) E.L.T. 613 held that parts of machines are also eligible for MODVAT credit as inputs. The decision was rendered in respect of a case prior to introduction of modvat on capital goods under Modvat Scheme. However, this goes to show the wide scope given to the term inputs.

ILLUSTRATIVE LIST OF JUDICIAL DECISIONS ON INPUT CREDIT UNDER MODVAT/CENVAT

Input (1)	Final product (2)	Eligibility (3)	Authority (4)
Alumina pellets/ Regenetal	Oxygen Acetylene	Yes	<i>CCE v. Indian Oxygen Ltd</i> 1995 (78) E.L.T. 270 (T-SZB)
Abrasive Emery Paper	In general	No	<i>Bajaj Auto Ltd. v. CCE</i> 1998 (101) E.L.T. 638 (T-WZB)
Clock assembly, radio, audio system	'Deluxe' model of Maruti car	Yes	<i>Maruti Udyog Ltd v. CCE</i> 1999 (107) E.L.T. 118 (T-NZB)
Cutting oil & quenching oil	Forgings	Yes	<i>Bharat Forges Ltd v. CCE</i> 1999 (112) E.L.T. 68 (T-WZB)
Electrodes	Used in welding machines for spot welding	Yes	<i>Bajaj Auto Ltd v. CCE</i> 1998 (99) E.L.T. 479 (T-WZB)
Explosives	Cement	Yes	Being used in relation to manufacture. <i>Jaypee Rewa Cement v. CCE</i> 2001 (133) E.L.T. 3 (SC)
Filter bags	Sugar	No	<i>Gwalior Sugar Co. Ltd v. CCE</i> 1992 (59) E.L.T. 482 (T-NZB)
Luggage carrier	Tata Sumo	Yes	<i>Telco Ltd v. CCE</i> 1999 (106) E.L.T. 84 (T-WZB SM)

Inputs used in or in relation to manufacture : Rule 2(k) specifies that credit of specified duty shall be allowed only on those inputs which are used in or in relation to the manufacture of final products whether directly or indirectly and whether contained in the final product or not.

The Cenvat scheme allows credit on inputs used in or in relation to the manufacture of final products. The Supreme Court in case of *J.K. Cotton Spinning and Weaving Mills Co. Ltd v. S.T.O.* 1997 (91) E.L.T. 34, has held that the expression “in the manufacture of goods” should normally encompass the entire process carried on by the dealer of converting raw materials into finished goods. Where any particular process of activity is so integrally related to the ultimate manufacture of goods, so that, without that process or activity manufacture may, even if theoretically possible, be commercially inexpedient, goods intended for use in the said process or activity would fall within the expression “in the manufacture of goods”. They need not be ingredients of commodities used in the process, nor must they be directly and actually needed for turning out the creation of goods. This decision is rendered in relation to sales tax legislation, still it is frequently used in modvat cases also.

In *Collector v. East End Paper Industries Ltd* - 1989 (43) E.L.T. 201 the Supreme Court held that anything that enters into and forms the part of the manufacturing process or is required to make the article marketable must be deemed to be a raw material or component part of the end product and must be deemed to have been used in completion or manufacture of the end product. In this specific case, wrapping paper was held to be a raw material and component of wrapped paper.

It is also clear from Rule 2(k) that the inputs may be used directly or indirectly. In *CCE v. Rajasthan Chemical Works* - 1991 (55) E.L.T. 444 the Supreme Court while deciding on the scope of the term ‘in relation of manufacture’ held that even processes like handling of raw materials would be a process in relation to manufacture if it is integrally connected with further operations leading to manufacture of end products.

In *Telco v. State of Bihar* - 1994 (74) E.L.T. 193, the Supreme Court held that the term raw material varies from industry to industry and decided that items like batteries, tyres and tubes, which, though are finished products in themselves, can be considered as raw materials for vehicles. Similarly, in *CCE v. Jay Engg. Works Ltd.* - 1989 (39) E.L.T. 169, the Supreme Court held that name plate fixed on a fan is an input eligible for set off under Notification 201/79 in view of the fact that without the said name plate the fans cannot be marketed.

Definition clearly says that inputs need not be contained in the final product. In *CCE v. Ballarpur Industries Ltd* - 1989 (43) E.L.T. 804, the Supreme Court held that sodium sulphate used for chemical reaction at pulp stage is treatable as raw material used in the manufacture of paper even though, sodium sulphate is burnt up and does not retain its identity in the end product. The Supreme Court specifically held that the test would be to

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see whether without the presence of the said raw material it would be possible to manufacture the end product.

The Madras High Court in *Ponds India Ltd v. Collector* - 1993 (63) E.L.T. 3 has held that the words "in relation to" must be given an extended meaning. Consequently, all processes which are preparatory in nature, but without which the manufacturing process cannot carry on would also be in relation to manufacture.

In *Indian Farmers Fertilisers Co-op Ltd v. CCE* - 1996 (86) E.L.T. 177, the Supreme Court had to decide whether raw naphtha used in offsite plants to produce ammonia which is in turn is used in water treatment plant, steam generation plant, effluent treatment plant and inert gas generation plant, could be eligible for the benefits of exemption notification which was issued exempting ammonia used for manufacture of fertilizers. The Supreme Court specifically held that water treatment plant, steam generation and inert gas generation plant are necessary parts of the process of manufacture of urea. They also held that pollution control plant is a part and parcel of the manufacturing process, in view of the emphasis laid on environmental protection.

Rule 2(k) allows credit on packing materials. There seems to be no restriction on those packing materials which do not enter the assessable value. Madras High Court in *Ponds India Ltd v. CCE* 1993 (63) E.L.T. 3 held that the term packaging materials means not only ready to use packages but also raw materials used to manufacture such packages.

Raw materials used for making cartons eligible for MODVAT - *Britannia Industries Ltd v. CCE* 1993 (67) E.L.T. 980 (T-EZB) -

Oil paint used to mark under Rule 51 on packages eligible - *Sterlite Inds Ltd v. CCE* 1995 (75) E.L.T. 712 (T-WZB)

Duplex boards used for producing cartons which was used to pack torches is eligible for MODVAT - *Geep Indl Syndicate Ltd v. CCE* 1995 (76) E.L.T. 399 (T-NZB)

Cellophane tapes used for sealing cartons eligible - *Kashmir Vanaspati Ltd v. CCE* 1996 (85) E.L.T. 150 (T-NZB SM)

4.3.7 Input service: Rule 2(l) defines input service as any service

- (i) used by a provider of taxable service for providing an output service; or
- (ii) used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products *upto* the place of removal,

and includes services used in relation to setting up, modernization, renovation or repairs of a factory, premises of provider of output service or an office relating to such factory or premises, advertisement or sales promotion, market research, storage upto the place of removal, procurement of inputs, activities relating to business, such as accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking,

credit rating, share registry, and security, inward transportation of inputs or capital goods and outward transportation upto the place of removal.

4.3.8 Input Service Distributor: Rule 2(m) defines input service distributor as an office of the manufacturer or producer of final products or provider of output service, which receives invoices issued under rule 4A of the Service Tax Rules, 1994 towards purchases of input services and issues invoice, bill or, as the case may be, challan for the purposes of distributing the credit of service tax paid on the said services to such manufacturer or producer or provider, as the case may be.

4.3.9 Job Work: Job work has been defined in Rule 2(n) as processing or working upon of raw material or semi-finished goods supplied to the job worker, so as to complete a part or whole of the process resulting in the manufacture or finishing of an article or any operation which is essential for aforesaid process and the expression "job worker" shall be construed accordingly.

4.3.10 Large tax payer: Rule 2(na) defines large tax payer to have the meaning assigned to it in the Central Excise Rules, 2002. The concept relating to large tax payer has been dealt in Chapter 5 : General Procedures Under Central Excise of Section A of this Study Material. .

4.3.11 Manufacturer or Producer: Manufacturer or producer in relation to articles of jewellery falling under heading 7113 of the First Schedule to the Central Excise Tariff Act includes a person who is liable to pay duty of excise leviable on such goods under sub-rule (1) of rule 12AA of the Central Excise Rules, 2002 [Rule 2(naa)].

4.3.12 Output service: Rule 2(p) defines output service as any taxable service excluding the taxable service referred to in sub-clause (zzp) of clause (105) of section 65 of the Finance Act (i.e. goods transport agency service) provided by the provider of taxable service, to a customer, client, subscriber, policy holder or any other person, as the case may be, and the expressions 'provider' and 'provided' shall be construed accordingly.

Here, "provider of taxable service" shall include a person liable for paying service tax. "Person liable for paying service tax" has the meaning as assigned to it in clause (d) of sub-rule (1) of rule 2 of the Service Tax Rules, 1994.

4.3.13 Second stage dealer: Rule 2(s) defines "second stage dealer" as a dealer who purchases the goods from a first stage dealer.

4.4 RULE 3 – CENVAT CREDIT

Sub-rule (1) of Rule 3 allows a manufacturer or producer of final products or a provider of taxable service to take Cenvat credit of

- i. the duty of excise specified in the First Schedule to the Tariff Act, leviable under the Act; (basic excise duty)

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- ii. the duty of excise specified in the Second Schedule to the Tariff Act, leviable under the Act; (special excise duty)
- iii. the additional duty of excise leviable under section 3 of the Additional Duties of Excise (Textile and Textile Articles) Act, 1978;
- iv. the additional duty of excise leviable under section 3 of the Additional Duties of Excise (Goods of Special Importance) Act, 1957;
- v. the national calamity contingent duty leviable under section 136 of the finance act, 2001 as amended by section 169 of the Finance Act 2003;
- vi. the education cess on excisable goods leviable under the Finance (No.2) Act, 2004;
- vii. the secondary and higher education cess on excisable goods leviable under the Finance Act, 2007;
- viii. the additional duty leviable under section 3 of the Customs Tariff Act, equivalent to the duty of excise specified under clauses (i), (ii), (iii), (iv), (v), (vi), and (vii);
- ix. the additional duty leviable under section 3(5) of the Customs Tariff Act. It is levied to counter balance the sales tax, value added tax, local tax etc. leviable on a like article on its sale, purchase or transportation in India. However, a provider of taxable service shall not be eligible to take credit of such additional duty.
- x. the additional duty of excise leviable under the Finance Act, 2003;
- xi. the service tax leviable under the Finance Act; and
- xii. the education cess on taxable services leviable under the Finance (No.2) Act, 2004; and
- xiii. the secondary and higher education cess on taxable services leviable under the Finance Act, 2007; and
- xiv. the additional duty of excise leviable on pan masala and tobacco products under the Finance Act, 2005

paid on-

- (i) any input or capital goods received in the factory of manufacture of final product or premises of the provider of output service on or after the 10th day of September, 2004; and
- (ii) any input service received by the manufacturer of final product or by the provider of output services on or after the 10th day of September, 2004.

Cenvat credit is also allowed in respect of the said duties, tax or cess paid on any inputs or input service used in the manufacture of intermediate products, by a job-worker availing the benefit of exemption specified in the *Notification No. 214/86* and received by the

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manufacturer for use in, or in relation to, the manufacture of final products on or after 10.9.2004.

Further, the amount equal to excise duty paid on the capital goods at the time of debonding of a unit in terms of the para 8 of Notification No. 22/2003 CE dated 31.03.2003 (which exempts certain goods when brought into 100% EOU / STP complex) shall be allowed as CENVAT credit. It may be noted here that in this case the credit is allowed for an amount equal to excise duty and not for excise duty.

It has been clarified that the manufacturer of the final products and the provider of output service shall be allowed Cenvat credit of additional duty leviable under section 3 of the Customs Tariff Act on goods falling under heading 9801 of the First Schedule to the Customs Tariff Act.

Sub-rule (2) lays down that in respect of goods which are exempt from duty or are non-excisable goods, if any duty has been paid on inputs lying in stock or in process or inputs contained in the final products lying in stock, Cenvat Credit in respect of such duty will be allowed to the manufacturer or producer of final products on the date on which such goods cease to be exempted goods or such goods become excisable.

Sub-rule (3) lays down that in respect of services which are exempt from service tax, if any duty has been paid on inputs (received on and after the 10th day of September, 2004) lying in stock and used for providing such service, Cenvat Credit in respect of such duty will be allowed to the provider of output service on the date on which such service ceases to be an exempted service.

As per Rule 3(4), Cenvat credit can be utilised for:

- (1) payment of duty of excise levied on any final products.
- (2) payment of duty on inputs removed as such or after being partially processed or capital goods removed as such.
- (3) payment of duty when duty paid goods are returned to factory and are subsequently removed after being remade, refined or reconditioned.
- (4) for payment of service tax on any output service.

However, while paying excise duty or service tax, the Cenvat Credit shall be utilised only to the extent such credit is available on the last day of the month or quarter for payment of duty or tax relating to that month or the quarter.

It may be noted that

- (a) the CENVAT credit of the duty, or service tax, paid on the inputs, or input services, used in the manufacture of final products cleared after availing of the exemption under the following Notifications

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- (i) No. 32/99-CE, dated 8th July, 1999
- (ii) No. 33/99-CE dated 8th July, 1999
- (iii) No. 39/2001-CE, dated 31st July, 2001
- (iv) No. 56/2002-CE, dated 14th November, 2002
- (v) No. 57/2002-CE, dated 14th November, 2002
- (vi) No. 56/2003-CE, dated 25th June, 2003 and
- (vii) No. 71/2003-CE, dated 9th September, 2003

shall, respectively, be utilized only for payment of duty on final products, in respect of which exemption under the said respective notifications is availed of.

- (b) No credit of the additional duty leviable under of section 3(5) of the Customs Tariff Act shall be utilised for payment of service tax on any output service.
- (c) CENVAT credit of only National Calamity Contingent duty (NCCD) shall be utilised for payment of the said NCCD payable on mobile phones.
- (d) CENVAT credit of only additional duty of excise leviable on pan masala and tobacco products under the Finance Act, 2005 shall be utilised for payment of said additional duty of excise on final products.

Rule 3(5) states that if the inputs or capital goods on which Cenvat credit has been taken are removed as such from the factory or premises of the provider of output service, the manufacturer of the final products or provider of output service shall pay an amount equal to the credit availed in respect of such inputs or capital goods. Such removal shall be made under the cover of an invoice referred to in Rule 9.

However, such payment shall not be required to be made where any inputs or capital goods are removed outside the premises of the provider of output service for providing the output service.

If the capital goods, on which CENVAT credit has been taken, are removed after being used, the manufacturer or provider of output service shall pay an amount equal to the CENVAT credit taken on the said capital goods reduced by 2.5% for each quarter of a year or part thereof from the date of taking the CENVAT credit.

Sub-rule (5A) provides that if the capital goods are cleared as waste and scrap, the manufacturer shall pay an amount equal to the duty leviable on transaction value.

Sub-rule (5B) provides that if the value of any

- (i) input, or
- (ii) capital goods before being put to use,

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on which CENVAT credit has been taken is written off fully or where any provision to write off fully has been made in the books of account, then the manufacturer *or service provider* shall pay an amount equivalent to the CENVAT credit taken in respect of the said input or capital goods.

However, if the said input or capital goods is subsequently used in the manufacture of final products *or the provision of taxable services*, the manufacturer *or output service provider* shall be entitled to take the credit of the amount equivalent to the CENVAT credit paid earlier subject to the other provisions of these rules.

Sub-rule (5C) provides that where on any goods manufactured or produced by an assessee, the payment of duty is ordered to be remitted under rule 21 of the Central Excise Rules, 2002, the CENVAT credit taken on the inputs used in the manufacture or production of said goods shall be reversed.

Sub-rule (6) lays down that amount paid under sub-rule (5) and sub-rule (5A) shall be eligible as Cenvat credit as if it was a duty paid by the person who removed such goods under sub-rule (5) and sub-rule (5A).

Sub-rule (7) lays down the method of calculating the amount of Cenvat Credit available in respect of inputs or capital goods produced or manufactured in a 100% Export Oriented Unit or by a unit in a Electronic Hardware Technology Park or Software Technology Park, and used in the manufacture of the final products or in providing output service in any other place in India.

$$\text{Cenvat Credit} = [X \times \{(1 + \text{BCD}/200) \times \text{CVD}/100\}]$$

Where BCD = the ad valorem rate of basic customs duty

CVD = the ad valorem rate of additional duty of customs

X = assessable value

Manner of utilisation of Cenvat credit

(1) Clause (b) of sub-rule 7 further lays down the manner of utilisation of Cenvat Credit. It provides that Cenvat credit in respect of -

- (i) the additional duty of excise leviable under section 3 of the Additional Duties of Excise (Textiles and Textile Articles) Act, 1978 ;
- (ii) the national calamity contingent duty leviable under the Finance Act, 2001;
- (iii) the education cess on excisable goods leviable under the Finance (No.2) Act, 2004;
- (iv) the secondary and higher education cess on excisable goods leviable under the Finance Act, 2007;
- (v) the additional duty leviable under section 3 of the Customs Tariff Act, equivalent to the duty of excise specified under items (i), (ii) and (iii) above;

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- (vi) the additional duty of excise leviable under the Finance Act, 2003;
- (vii) the education cess on taxable services leviable under the Finance (No.2) Act, 2004;
- (viii) the secondary and higher education cess on taxable services leviable under the Finance Act, 2007; and
- (ix) the additional duty of excise leviable under the Finance Act, 2005,

shall be utilized only towards payment of duty of excise or as the case may be, of service tax leviable under the said Additional Duties of Excise (Textiles and Textile Articles) Act, 1978 or the national calamity contingent duty, or the education cess on excisable goods, or the secondary and higher education cess on excisable goods, or the additional duty of excise leviable under the Finance Act, 2003, or the education cess on taxable services or the secondary and higher education cess on taxable services or the additional duty of excise leviable under the Finance Act, 2005, respectively, on any final products manufactured by the manufacturer or for payment of such duty on inputs themselves, if such inputs are removed as such or after being partially processed or on any output service.

However, credit of the education cess on excisable goods and education cess on taxable services can be utilised, either for payment of the education cess on excisable goods or for the payment of the education cess on taxable services.

Also, the credit of the secondary and higher education cess on excisable goods and the secondary and higher education cess on taxable services can be utilized, either for payment of the secondary and higher education cess on excisable goods or for the payment of the secondary and higher education cess on taxable services.

It has been clarified that the credit of the additional duty of excise leviable under section 3 of the Additional Duties of Excise (Goods of Special Importance) Act, 1957 paid on or after the 1st day of April, 2000, may be utilised towards payment of duty of excise leviable under the First Schedule or the Second Schedule to the Excise Tariff Act. Thus, Basic excise duty, Special excise duty and the Additional excise duty (GSI) are inter-changeable i.e. credit of duty paid under one head can be utilised for payment of duty under other head.

(2) The Cenvat credit, in respect of additional duty leviable under section 3 of the Customs Tariff Act, paid on marble slabs or tiles falling under tariff items 2515 12 20 and 2515 12 90 respectively of the First Schedule to the Tariff Act shall be allowed to the extent of Rs.30 per square metre.

It has been explained that where the provisions of any other rule or notification provide for grant of whole or part exemption on condition of non-availability of credit of duty paid on any input or capital goods, or of service tax paid on input service, the provisions of such other rule or notification shall prevail over the provisions of these rules.

Though there is no reference to waste, refuse or by-product, the *C.B.E.C. Circular No.B/4/7/2000-TRU, dated 3.4.2000* has clarified that cenvat credit shall be admissible on

the part of the input contained in waste, refuse or by-product. Further, the guidelines issued by the Board on 1st September 2001 reiterate the same.

4.5 RULE 4 – CONDITIONS FOR AVAILING THE CENVAT CREDIT

Rule 4 specifies the conditions for allowing CENVAT credit. Sub-rule 1 allows instant credit on inputs after receipt into the factory of the manufacturer or in the premises of the provider of output service. Two points to be noted here are that the manufacturer/output service provider can take the credit immediately as soon as the inputs are received in the factory/premises:

- (i) without waiting till the inputs are actually utilized in the manufacture and
- (ii) even if the payment for the inputs to the supplier is pending

However, in case of input services, CENVAT credit can be taken only after the payment of value of taxable services and service tax as indicated in the invoice, to the service provider.

The proviso to rule 4(1) lays down that where articles of jewellery (falling under heading 7113 of the Central Excise Tariff) are manufactured on job work basis, the CENVAT credit of duty paid on inputs may be taken immediately on receipt of such inputs in the registered premises of the principal manufacturer subject to the condition that such inputs are used in the manufacture of articles of jewellery by the job worker.

Credit in case of trade discount: Sometimes a manufacturer may avail full credit of the amount of duty paid by supplier as reflected in the invoice. However, subsequently the supplier allows some trade discount or reduces the price, without reducing the duty paid by him. In such a case, the entire amount of duty paid by the manufacturer, as shown in the invoice would be available as credit for the reason that rule 3 of CENVAT Credit Rules, 2004 allows credit of duty “paid” by the inputs manufacturer and not duty “payable” by the said manufacturer. It may however be confirmed that the supplier, who has paid duty, has not filed/claimed the refund on account of reduction in price.

However, if the duty paid is also reduced, along with the reduction in price, the reduced excise duty would only be available as credit [Circular No. 877/15/2008-CX dated 17.11.2008].

Sub-rule 2(a) however restricts the quantum of credit in respect of capital goods received in a factory or in the premises of the provider of output service at any point of time in a given financial year as under:

- a. Upto 50% in the same financial year;
- b. Balance in one or more subsequent financial years provided the capital goods is still in the possession and use of the manufacturer or the output service provider;

If the capital goods are cleared as such in the same financial year, Cenvat credit in respect of such capital goods shall be allowed for the whole amount of the duty paid on such capital

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goods in the same financial year.

Further, the CENVAT credit of the additional duty leviable under section 3(5) of the Customs Tariff Act in respect of capital goods shall be allowed immediately on receipt of the capital goods in the factory of a manufacturer.

In respect of certain capital goods like components, spares and accessories, refractories and refractory materials, moulds and dies and goods falling under heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804 of the Central Excise Tariff, the condition regarding possession of the capital goods in the second year is not there since these are consumable items, provided they are not sold.

Illustration.- A manufacturer received machinery on the 16th day of April, 2002 in his factory. Cenvat of two lakh rupees is paid on this machinery. The manufacturer can take credit upto a maximum of one lakh rupees in the financial year 2002-2003, and the balance in subsequent years..

Sub-rule (3) allows Cenvat credit for capital goods acquired on lease, hire-purchase or through loan from a financing company.

Sub-rule (4) provides that no Cenvat credit shall be allowed in respect of that part of the value of capital goods which represents the amount of duty on such capital goods, which the manufacturer or provider of output service claims as depreciation under section 32 of the Income-tax Act, 1961.

In other words the manufacturer or provider of output service cannot enjoy the benefit of both depreciation allowance as well as Cenvat Credit.

Sub-rule 7 provides that Cenvat credit in respect of input service shall be allowed, on or after the day which payment is made of the value of input service and the service tax paid or payable as is indicated in invoice, bill or, as the case may be, challan referred to in rule 9.

4.6 JOB WORK PROVISIONS [RULE 4(5) AND 4(6)]

The goods (being inputs or capital goods) may be sent to the job worker for further processing, testing, repair, reconditioning or for the manufacture of intermediate goods necessary for the manufacture of final products or any other purpose. Rule 4(5) lays down that in order to avail Cenvat credit on such goods a time limit of 180 days has been fixed before which the goods must be ordinarily returned to the factory. In case the goods are not returned within 180 days the credit on such goods has to be reversed. However, credit can be retaken once the goods come back.

Sub-rule 5(b) extends the Cenvat credit in respect of moulds, dies, jigs and fixtures sent by a manufacturer of final products to a job worker for production of goods on his behalf according to his specifications without any time limit for its return.

Sub-rule (6) allows direct despatch or clearance of final products from job worker's premises subject to the approval of Deputy Commissioner of Central Excise or Assistant Commissioner of Central Excise, as the case may be, in each such case of removal. This approval can be granted on an annual basis to each job worker.

4.7 RULE 5 – REFUND OF CENVAT CREDIT

This rule provides a benefit for inputs or input services that are used

- (i) in the manufacture of final product which is cleared for export under bond or letter of undertaking (LUT), or
- (ii) in the intermediate product cleared for export, or
- (iii) in providing output service which is exported.

The CENVAT credit in respect of the input or input service so used shall be allowed to be utilized by the manufacturer or provider of output service towards payment of,

- (i) duty of excise on any final product cleared for home consumption or for export on payment of duty; or
- (ii) service tax on output service,

Where for any reason such adjustment is not possible, the manufacturer or the provider of output service shall be allowed refund of such amount subject to such safeguards, conditions and limitations, as may be specified, by the Central Government, by notification. It is important to note here that cash refund of CENVAT is possible only for exports and not for home clearance.

However, no refund of credit shall be allowed if the manufacturer or provider of output service avails of drawback allowed under the Customs and Central Excise Duties Drawback Rules, 1995, or claims rebate of duty under the Central Excise Rules, 2002, in respect of such duty; or claims rebate of service tax under the Export of Service Rules, 2005 in respect of such tax.

Further no credit of the additional duty leviable under sub-section (5) of section 3 of the Customs Tariff Act shall be utilised for payment of service tax on any output service.

Here, 'output service which is exported' means the output service exported in accordance with the Export of Services Rules, 2005.

The safeguards, conditions and limitations, subject to which the refund under Rule 5 of CENVAT Credit Rules, 2004 shall be granted, are as follows:

1. The final product or the output service is exported in accordance with the procedure laid down in the Central Excise Rules, 2002, or the Export of Services Rules, 2005, as the case may be.
2. The claims for such refund are submitted not more than once for any quarter in a

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calendar year. However, where,-

(a) the average export clearances of final products or the output services in value terms is 50% or more of the total clearances of final products or output services, as the case may be, in the preceding quarter; or

(b) the claim is filed by Export Oriented Unit,

the claim for such refund may be submitted for each calendar month.

3. The manufacturer or provider of output service, as the case may be, submits an application in the prescribed Form to the Deputy/Assistant Commissioner of Central Excise, as the case may be, in whose jurisdiction,-

(a) the factory from which the final products are exported is situated, along with the Shipping Bill or Bill of Export, duly certified by the officer of customs or a photocopy thereof duly attested by him to the effect that goods have in fact been exported; or

(b) the registered premises of the service provider from which output services are exported is situated, along with a copy of the invoice and a certificate from the bank certifying realization of export proceeds

4. The refund is allowed only in those circumstances where a manufacturer or provider of output service is not in a position to utilize the input credit or input service credit allowed under rule 3 of the said rules against goods exported during the quarter or month to which the claim relates (hereinafter referred to as 'the given period').

5. The refund of unutilised input service credit will be restricted to the extent of the ratio of export turnover to the total turnover for the given period to which the claim relates i.e.

Maximum refund = Total CENVAT credit taken on input services during the given period × export turnover ÷ Total turnover

Illustration: If total credit taken on input services for a quarter = Rs. 100

Export turnover during the quarter = Rs 250

Total Turnover during the quarter = Rs 500

Refund of input service credit under Rule 5 of the CENVAT Credit Rule, during the quarter = $100 \times 250 / 500$ i.e. Rs 50

Explanation: For the purposes of condition no.5,-

1. "Export turnover" shall mean the sum total of the value of final products and output services exported during the given period in respect of which the exporter claims the facility of refund under this rule.

2. "Total turnover" means the sum total of the value of,-
 - (a) all output services and exempted services provided, including value of services exported;
 - (b) all excisable and non excisable goods cleared, including the value of goods exported;
 - (c) the value of bought out goods sold, during the given period.
6. The application in the prescribed form along with the prescribed enclosures and the relevant extracts of the records maintained under the Central Excise Rules, 2002, CENVAT Credit Rules, 2004, or the Service Tax Rules, 1994, in original, are filed with the Deputy/Assistant Commissioner of Central Excise, as the case may be, before the expiry of the period specified in section 11B of the Central Excise Act, 1944.
7. The refund of excise duty or service tax is allowed by the Deputy/Assistant Commissioner of Central Excise, as the case may be.

4.8 RULE 5A – REFUND OF CENVAT CREDIT TO UNITS IN SPECIFIED AREAS

The Central Government may allow refund of CENVAT credit of duty taken on inputs used in the manufacture of final products cleared in terms of *Notification No. 20/2007-CE dated 25.04.2007* if the manufacturer is unable to utilize such credit for paying duty on such final products.

However, the refund shall not be allowed if the final products are exempt or subject to nil rate of duty. The refund of credit shall be allowed subject to prescribed procedures, conditions and limitations.

For the purposes of this rule, "duty" means the duties specified in sub-rule (1) of rule 3 of these rules.

Notification No. 20/2007 CE dated 25.04.2007 has granted exemption to certain specified goods cleared from a unit located in the States of Assam or Tripura or Meghalaya or Mizoram or Manipur or Nagaland or Arunachal Pradesh or Sikkim from so much of the duty of excise leviable thereon as is equivalent to the amount of duty paid by the manufacturer of goods other than the amount of duty paid by utilization of CENVAT credit under the CENVAT Credit Rules, 2004.

4.9 RULE 6 - OBLIGATION OF MANUFACTURER OF DUTIABLE AND EXEMPTED GOODS AND PROVIDER OF TAXABLE AND EXEMPTED SERVICES

Rule 6(1) provides that Cenvat credit shall not be allowed on such input or input service which is used in the manufacture of exempted goods or for provision of exempted services.

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The credit to the extent taken on inputs used for exempted products and exempted services must be reversed subject to the Rule 6(2). CBE&C has clarified vide its Circular No. 754/70/2003-CX dated 9.10.2003 that no credit can be taken on inputs which are used exclusively in or in relation to the manufacture of exempted final products.

However, the CENVAT credit on inputs shall not be denied to job worker referred to in rule 12AA of the Central Excise Rules, 2002, on the ground that the said inputs are used in the manufacture of goods cleared without payment of duty under the provisions of that rule.

Rule 6(2) prescribes the maintenance of separate set of books of accounts in cases where a manufacturer or provider of output service avails of CENVAT credit in respect of any inputs or input services and manufactures dutiable final products or provides taxable output service as well as exempted goods or services. The manufacturer or the provider of output service may maintain separate accounts for receipts, consumption and inventory of inputs and input services meant for use in the manufacture of dutiable final products or in providing taxable output service and the quantity of inputs meant for use in the manufacture of exempted goods or services. He may then take CENVAT credit only on that quantity of inputs or input services which are intended for use in the manufacture of dutiable goods or in providing output service on which service tax is payable.

Rule 6(3) gives an option to the manufacturer or the provider of output service opting not to maintain separate accounts to do any of the following:

- (i) the manufacturer of goods shall pay an amount equal to 5% of value of the exempted goods and the provider of output service shall pay an amount equal to 6% of value of the exempted services; or
- (ii) the manufacturer of goods or the provider of output service shall pay an amount equivalent to the CENVAT credit attributable to inputs and input services used in, or in relation to, the manufacture of exempted goods or for provision of exempted services subject to the conditions and procedure specified in sub-rule (3A).

If the manufacturer of goods or the provider of output service, avails any of the option under this sub-rule, he shall exercise such option for all exempted goods manufactured by him or, as the case may be, all exempted services provided by him, and such option shall not be withdrawn during the remaining part of the financial year [Explanation I].

The credit shall not be allowed on inputs and input services used exclusively for the manufacture of exempted goods or provision of exempted service [Explanation II].

Sub-rule (3A) prescribes the conditions and procedure for determination and payment of amount payable under clause (ii) of sub-rule (3) above. It provides that the manufacturer of goods or the provider of output service shall follow the following procedure and conditions, namely:-

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- (a) The following particulars are to be furnished in writing to the Superintendent of Central Excise:-
- (i) name, address and registration number;
 - (ii) date from which the option is exercised or proposed to be exercised;
 - (iii) description of dutiable goods or taxable services;
 - (iv) description of exempted goods or exempted services;
 - (v) CENVAT credit of inputs and input services lying in balance as on the date of exercising the option;
- (b) Determine and pay, provisionally, for every month-
- (i) the amount equivalent to CENVAT credit attributable to inputs used in or in relation to manufacture of exempted goods, denoted as A;
 - (ii) the amount of CENVAT credit attributable to inputs used for provision of exempted services (provisional) = $(B/C) \times D$, where
 - B denotes the total value of exempted services provided during the preceding financial year,
 - C denotes the total value of dutiable goods manufactured and removed plus the total value of taxable services provided plus the total value of exempted services provided, during the preceding financial year and
 - D denotes total CENVAT credit taken on inputs during the month minus A;
 - (iii) the amount attributable to input services used in or in relation to manufacture of exempted goods or provision of exempted services (provisional) = $(E/F) \times G$, where
 - E denotes total value of exempted services provided plus the total value of exempted goods manufactured and removed during the preceding financial year,
 - F denotes total value of taxable and exempted services provided, and total value of dutiable and exempted goods manufactured and removed, during the preceding financial year, and
 - G denotes total CENVAT credit taken on input services during the month;
- (c) Determine the amount of CENVAT credit attributable to exempted goods and exempted services for the whole financial year in the following manner, namely:-
- (i) the amount of CENVAT credit attributable to inputs used in or in relation to manufacture of exempted goods, on the basis of total quantity of inputs used in or in relation to manufacture of said exempted goods, denoted as H;
 - (ii) the amount of CENVAT credit attributable to inputs used for provision of exempted services = $(J/K) \times L$, where

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- J denotes the total value of exempted services provided during the financial year,
- K denotes the total value of dutiable goods manufactured and removed plus the total value of taxable services provided plus the total value of exempted services provided, during the financial year and
- L denotes total CENVAT credit taken on inputs during the financial year minus H;
- (iii) the amount attributable to input services used in or in relation to manufacture of exempted goods or provision of exempted services = $(M/N) \times P$, where
- M denotes total value of exempted services provided plus the total value of exempted goods manufactured and removed during the financial year,
- N denotes total value of taxable and exempted services provided, and total value of dutiable and exempted goods manufactured and removed, during the financial year, and
- P denotes total CENVAT credit taken on input services during the financial year;
- (d) Pay (c) minus (b) on or before the 30th June of the succeeding financial year, where (c) > (b);
- (e) Also pay interest at the rate of 24% p.a. from the due date, i.e., 30th June till the date of payment, where the amount short-paid is not paid by the said due date;
- (f) If (c) is less than (b), adjust the excess amount on his own, by taking credit of such amount;
- (g) Intimate the following particulars to the jurisdictional Superintendent of Central Excise, within 15 days from the date of payment or adjustment:-
- (i) details of CENVAT credit attributable to exempted goods and exempted services, monthwise, for the whole financial year, determined provisionally as per (b),
 - (ii) CENVAT credit attributable to exempted goods and exempted services for the whole financial year, determined as per (c),
 - (iii) amount short paid determined as per (d), alongwith the date of payment of the amount short-paid,
 - (iv) interest payable and paid, if any, on the amount short-paid, determined as per condition (e), and
 - (v) credit taken on account of excess payment, if any, determined as per (f);
- (h) If (b) cannot be determined provisionally due to reasons that no dutiable goods were manufactured and no taxable service was provided in the preceding financial year, then it is not required to determine and pay such amount provisionally for each month, but determine the CENVAT credit attributable to exempted goods or exempted services for the whole year as per (c) and pay the amount so calculated on or before 30th June of the succeeding financial year;

- (i) Where the amount as per (h) is not paid by the due date, i.e., 30th June, then pay interest at the rate of 24% p.a. from the due date till the date of payment.

“Value” for the purpose of sub-rules (3) and (3A) shall have the same meaning assigned to it under section 67 of the Finance Act, 1994 read with rules made thereunder or, as the case may be, the value determined under section 4 or 4A of the Central Excise Act, 1944 read with rules made thereunder [Explanation I].

The amount mentioned in sub-rules (3) and (3A), unless specified otherwise, shall be paid by debiting the CENVAT credit or otherwise on or before the 5th day of the following month except for the month of March, when such payment shall be made on or before the 31st March [Explanation II].

If the manufacturer of goods or the provider of output service fails to pay the amount payable under sub-rule (3) or sub-rule (3A), it shall be recovered, in the manner as provided in rule 14, for recovery of CENVAT credit wrongly taken [Explanation III].

Sub-rule (4) specifies that no Cenvat credit would be allowed on capital goods used exclusively in the manufacture of exempted goods or in providing exempted services, other than the final products which are exempt under any notification on the basis of the value or quantity of clearances made in a financial year. This would mean that for the clearances undertaken through *Notification 8/2003*, Cenvat credit on capital goods can be availed, though the utilisation will be subject to the conditions of that notification.

Sub-rule (5) lays down that if the following input services are used commonly, either in the manufacture of both dutiable as well as exempted goods or in rendering taxable as well as exempted goods, the obligations prescribed under the rules, will not be attracted. However, if these services are exclusively used either in the manufactured of exempted goods or in rendering exempted service, no credit can be availed.

- (i) Consulting engineer.
- (ii) Architect.
- (iii) Interior decorator.
- (iv) Management consultant.
- (v) Real estate agent.
- (vi) Security agency.
- (vii) Scientific or technical consultancy.
- (viii) Banking and other financial services.
- (ix) Insurance auxiliary services.
- (x) Erection, commissioning and Installation agency.
- (xi) Maintenance or repair.

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- (xii) Technical testing and analysis.
- (xiii) Technical inspection and certification.
- (xiv) Foreign exchange brokers.
- (xv) Construction service.
- (xvi) Intellectual property service.

Sub rule (6) exempts the following clearances from the operation of sub rule 1 to 4 of this Rule. In other words, where common inputs are utilised for clearances of exempt products to the aforesaid categories, the need to follow the procedure of reversal need not be adhered to.

Category to whom supplied	
1.	Units in Special Economic Zone or to a developer of a special economic zone for their authorized operations
2.	Units in 100% EOU
3.	Units in Electronic Hardware Technology Park (EHTP)
4.	Units in Software Technology Park (STP)
5.	United Nations or International Organisations vide <i>Notification 108/95 CE dated 28.8.1995</i>
6.	Cleared for export under bond in terms of the provisions of the Central Excise Rules, 2002
7.	Gold or silver falling within Chapter 71 of the said First Schedule, arising in the course of manufacture of copper or zinc by smelting or.
8.	all goods which are exempt from the duties of customs leviable under the First Schedule to the Customs Tariff Act, 1975 and the additional duty leviable under section 3 of the said Customs Tariff Act when imported into India and supplied against International Competitive Bidding in terms of <i>Notification No. 6/2002 CE dated the 1st March, 2002.</i>

Circular No. 868/6/2008 CX dated 09.05.2008 has clarified the following issues with regard to rule 6 of the CENVAT Credit Rules, 2004:

1. **Issue:** Whether an assessee availing option (i) or option (ii) under rule 6(3) is allowed to take CENVAT credit of duty paid on inputs and input services which are used for both dutiable and exempted goods or services?

Clarification: Yes, credit on such inputs and input services is allowed. However, an assessee following option (i) or (ii) under rule 6(3) shall not be allowed to take CENVAT

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credit of duty paid on those inputs and input services which are used exclusively for the manufacture of exempted goods or provision of exempted services [refer Explanation 2 of rule 6(3)].

For the purpose of the calculation of amount under formula given under rule 6(3A), the total CENVAT credit taken on inputs and input services does not include excise duty paid on inputs or service tax paid on input services which are used exclusively for the manufacture of exempted goods or provision of exempted services.

2. **Issue:** Whether an assessee availing option (i) in respect of certain exempted goods/services can also avail option (ii) in respect of other exempted goods or services simultaneously?

Clarification: An assessee opting for either of the option is required to avail the said option for all the exempted goods manufactured by him and all the exempted services provided by him and the option once exercised during a financial year (F.Y.) cannot be withdrawn during the remaining part of the FY. Therefore, the same assessee cannot avail both option (i) and option (ii) simultaneously during a financial year. [Explanation 1 to Rule 6(3)].

3. **Issue:** Assessee opting for option (i) is required to pay an amount equivalent to 10% (now 5% w.e.f. 07.07.2009) of value of exempted goods or 8% (now 6% w.e.f. 07.07.2009) of value of exempted services. What is the scope of term "value" for the said purpose?

Clarification: Value of the exempted goods is the transaction value as determined in terms of section 4 of the Central Excise Act, 1944 or value determined under section 4A. However, in case of goods chargeable to specific rate of duty, the value, shall be the transaction value to be determined under section 4. Value of the exempted service is the gross amount charged for providing the exempted service [without abatement].

4. **Issue:** What is the accounting code to be followed by the assessee who is required to pay 8% (now 6% w.e.f. 07.07.2009) or other amount for the exempted service under rule 6(3)?

Clarification: For the present, the assessee can pay the said amount under the accounting code applicable for service tax i.e. 0044.

5. **Issue:** Whether input service distributor can also opt for option (i) or option (ii)?

Clarification: As input service distributor does not provide any service, and is like a trader, the question of availing either of the options would not arise.

6. **Issue:** Whether export of service without payment of service tax under Export of Service Rules shall be treated as exempted service for the purpose of rule 6(3)?

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Clarification: No, export of services without payment of service tax are not to be treated exempted services.

7. **Issue:** What is the manner for calculation of CENVAT Credit amount attributable to inputs used in or in relation to the manufacture of exempted goods?

Clarification: It is required to be done on the basis of actual consumption of inputs used and the quantification may be made based upon the stores/production records maintained by the manufacturer. Further, a certificate from Cost Accountant/Chartered Accountant giving details of quantity of inputs used in the manufacture of exempted goods, value thereof and CENVAT credit taken on these inputs may be submitted at the end of the year.

8. **Issue:** Whether credit in respect of input services covered by rule 6(5) would be required to be taken into account for determination of amount payable as per formula provide in rule 6(3A)?

Clarification: No, the credit attributable to services mentioned in sub-rule (5) shall not be taken into account for determination of amount under rule 6(3A).

4.10 OPTION TO PAY DUTY

An interesting question which arises is whether a manufacturer can continue to pay duty and avail Cenvat even if his product is exempt from duty. It is quite true that the Supreme Court has held in *CCE v. Parle Exports Ltd.* - 1988 (38) E.L.T. 741 that notifications are to be construed as part of the statute itself. The A.P. High Court in *Ganesh Metal Processing Industries v. UOI* - 1996 (81) E.L.T. 11 held in the context of Notification 202/88 that once an exemption notification exists Modvat credit cannot be availed and that clearance cannot be added. However, the Tribunal has been consistently holding (even after the AP High Court decision) that the assessee has an option to either go for Cenvat or to opt for exemption notification. Few examples of such cases are

- a. *Bansal Auto Parts Industries v. CCE* - 1998 (79) ECR 850 (T-NZB);
- b. *Everest Convertors v. CCE* - 1995 (80) E.L.T. 91(T-EZB);
- c. *Polychem Ltd. v. CCE* - 1997 (90) E.L.T. 156 (T-NZB),
- d. *Gothi Plastic Industries v. CCE* - 1996 (83) E.L.T. 123 (T-SZB);
- e. *Mechciv Engineers v. CCE* - 1997 (20) RLT 200 (T-NZB SM)

In view of the fact that the definition of “final products” contained in Rule 2 is wide enough to cover “exempted goods”, it seems as if this controversy is set to continue. The Department could take a stance that since there are two separate definitions for final products and exempted goods, one does not include the other.

4.11 RULE 7 – MANNER OF DISTRIBUTION OF CREDIT BY INPUT SERVICE DISTRIBUTOR

In real life situations, many a time the bill / invoice is raised in the name of head office/regional office etc. for services which are actually received in the factory (or factories) or premises of service provider. In addition, the bill for services which are not specific for any factory/premises, such as advertising, market research, management consultancy etc. would also be received only in these offices. Rule 7 tends to provide a way to distribute such credit to the factory or the premises of the output service provider. Rule 2(m) read with rule 7 defines an "input service distributor" as an office of manufacturer or provider of output service which receives invoices towards purchase of input services and issues invoice, bill or challan for the purpose of distributing the credit of service tax paid on the services to its manufacturing units or units providing output service. Thus the distributor is comparable to dealers under the CENVAT scheme of inputs and capital goods. The document issued by him is being accepted under law as eligible document under rule 9(1)(g) for availing credit. To pass on the credit, the input service distributor has to obtain service tax registration, comply with new rule 4A of Service Tax Rules and file half-yearly statement with the Superintendent under rule 9(10) of Cenvat rules 2004.

The input service distributor may distribute the Cenvat credit in respect of the service tax paid on the input service to its manufacturing units or units providing output service, subject to the following condition, namely:-

- (a) the credit distributed against a document referred to in rule 9 does not exceed the amount of service tax paid thereon; or
- (b) credit of service tax attributable to service use in a unit exclusively engaged in manufacture of exempted goods or providing of exempted services shall not be distributed.

4.12 RULE 7A – DISTRIBUTION OF CREDIT ON INPUTS BY THE OFFICE OR ANY OTHER PREMISES OF OUTPUT SERVICE PROVIDER

Sub-rule (1) lays down that a provider of output service shall be allowed to take credit on inputs and capital goods received, on the basis of an invoice or a bill or a challan issued by an office or premises of the said provider of output service, which receives invoices, issued in terms of the provisions of the Central Excise Rules, 2002, towards the purchase of inputs and capital goods.

Sub-rule (2) provides that the provisions of these rules or any other rules made under the Central Excise Act, 1944, as made applicable to a first stage dealer or a second stage dealer, shall mutatis mutandis apply to such office or premises of the provider of output service.

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4.13 RULE 8 – STORAGE OF INPUTS OUTSIDE THE FACTORY OF THE MANUFACTURER

The Assistant/Deputy Commissioner can also permit the inputs in respect of which Cenvat has been taken to be stored outside the factory of the manufacturer concerned. However, such storage of inputs outside the factory shall be allowed only in the exceptional circumstances having regard to the nature of the goods and shortage of storage space at the premises of such manufacturer, and shall be subject to suitable safeguards against any loss of revenue. Where such inputs are not subsequently brought into the factory for use in the manner prescribed in the Cenvat Credit Rules for any reason whatsoever, it has been stipulated that the manufacturer of the final products shall pay a duty of excise equal to the amount of credit that has been availed in respect of such inputs.

4.14 RULE 9 - DOCUMENTS AND ACCOUNTS

Sub-rule (1) allows manufacturer or the provider of output service or input service distributor to avail Cenvat credit on the basis of the following documents

Nature of document
1. Invoice issued by manufacturer for clearance of inputs or capital goods from his factory, his depot, premises of the consignment agent, any other premises from where the goods are sold by or on his behalf
2. Invoice issued by manufacturer for clearance of inputs or capital goods as such
3. Invoice issued by an importer
4. Invoices issued by an importer from his depot, premises of his consignment agent if the said depot or the premises are registered in terms of the provisions of the Central Excise Rules 2002.
5. Invoice issued by a first stage dealer or second stage dealer under Central Excise Rules, 2002
6. Bill of entry
7. Supplementary invoice issued by manufacturer or importer of inputs or capital goods for payment of additional duty of customs
8. Certificate issued by an appraiser of customs in respect of goods imported through a foreign post office.

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9. a challan evidencing payment of service tax by the person liable to pay service tax under sub-clauses (iii), (iv), (v) and (vii) of clause (d) of sub-rule (1) of rule (2) of the Service Tax Rules, 1994
10. an invoice, a bill or challan issued by a provider of input service on or after the 10th day of, September, 2004
11. an invoice, bill or challan issued by an input service distributor under rule 4A of the Service Tax Rules, 1994.

It may be noted that the credit of additional duty of customs levied under sub-section (5) of section 3 of the Customs Tariff Act, 1975 shall not be allowed if the invoice or the supplementary invoice, as the case may be, bears an indication to the effect that no credit of the said additional duty shall be admissible.

Sub-rule (2) provides that the CENVAT credit can be taken only if all the particulars as prescribed under the Central Excise Rules, 2002 or the Service Tax Rules, 1994 are available on the invoice or other duty-paying document.

However, the Deputy/Assistant Commissioner may allow the CENVAT credit even if the said document does not contain all the particulars but the following two conditions are satisfied:

- (a) The document contains the following information:
- details of duty or service tax payable,
 - description of the goods or taxable service,
 - assessable value,
 - central excise/service tax registration number of the person issuing the invoice
 - name and address of the factory or warehouse or premises of first or second stage dealers or provider of taxable service, and
- (b) The Deputy/Assistant Commissioner is satisfied that the:
- (i) goods or services covered by the said document have been received and
 - (ii) accounted for in the books of the account of the receiver.

Sub-rule (4) lays down that the Cenvat credit in respect of input or capital goods purchased from a first stage dealer or second stage dealer shall be allowed only if such first stage dealer or second stage dealer, as the case may be, has maintained records indicating the fact that the input or capital goods was supplied from the stock on which duty was paid by the producer of such input or capital goods and only an amount of such duty on pro rata basis has been indicated in the invoice issued by him.

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As per sub-rule (5), the manufacturer of final products or the provider of output service shall maintain proper records for the receipt, disposal, consumption and inventory of the input and capital goods in which the relevant information regarding the value, duty paid, Cenvat credit taken and utilized, the person from whom the input or capital goods have been procured is recorded and the burden of proof regarding the admissibility of the Cenvat credit shall lie upon the manufacturer or provider of output service taking such credit.

Sub-rule (6) specifies that the manufacturer of final products or the provider of output service shall maintain proper records for the receipt and consumption of the input services in which the relevant information regarding the value, tax paid, Cenvat credit taken and utilized, the person from whom the input service has been procured is recorded and the burden of proof regarding the admissibility of the Cenvat credit shall lie upon the manufacturer or provider of output service taking such credit.

The manufacturer of final products shall submit within ten days from the close of each month to the Superintendent of Central Excise, a monthly return in the form specified, by notification, by the Board. However, a manufacturer availing exemption under a notification based on the value or quantity of clearances in a financial year shall file a quarterly return in the form specified, by notification, by the Board within twenty days after the close of the quarter to which the return relates [Sub-rule 7].

A first stage dealer or a second stage dealer, as the case may be, shall submit within fifteen days from the close of each quarter of a year to the Superintendent of Central Excise, a return in the form specified, by notification, by the Board [Sub-rule 8].

Sub-rule (9) lays down that the provider of output service availing Cenvat credit, shall submit a half yearly return in form (ST-3) specified, by notification, by the Board to the Superintendent of Central Excise, by the end of the month following the particular quarter or half year.

Sub-rule (10) prescribes that the input service distributor, shall submit a half yearly return, giving the details of credit received and distributed during the said half year to the Superintendent of Central Excise, by the end of the month following the half year.

Sub-rule (11) allows the output service provider or the input service distributor to rectify mistakes or omission and file revised return within 60 days from the date of filing of original return.

4.15 RULE 9A – INFORMATION RELATING TO PRINCIPAL INPUTS

A manufacturer of final products has to furnish to the Superintendent of Central Excise a declaration in the prescribed Form (ER 5) in respect of the principal inputs and the quantity of such principal inputs required for use in the manufacture of unit quantity of each of the excisable goods manufactured or to be manufactured by him. Such declaration has to be filed annually by 30th April of each Financial Year. However, for the year 2004-05, such information can be furnished by 31st December, 2004.

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If a manufacturer of final products intends to make any alteration in the information so furnished he shall furnish information to the Superintendent of Central Excise together with the reasons for such alteration before the proposed change or within 15 days of such change in the prescribed Form.

Further, a manufacturer of final products has to submit, a monthly return in the prescribed Form (ER 6), in respect of information regarding the receipt and consumption of each principal inputs with reference to the quantity of final products manufactured by him. Such return shall be filed within 10 days from the close of each month, to the Superintendent of Central Excise.

The Central Government may, by notification and subject to such conditions or limitations, as may be specified in such notification, specify manufacturers or class of manufacturers who may not be required to furnish such declaration or monthly return.

The assessee who

- manufacture excisable goods falling under Chapters 22, 28 to 30, 32 to 34, 38 to 40, 48, 72 to 74, 76, 84, 85, 87, 90 and 94 and Heading Nos. 54.02, 54.03, 55.01, 55.02, 55.03 and 55.04 and
- have paid excise duty of Rs.100 lakh or more during the preceding financial year are required to submit the return ER-6. All other assessee are exempted from furnishing such return.

Here, principal inputs means any input which is used in the manufacture of final products where the cost of such input constitutes not less than 10% of the total cost of raw-materials for the manufacture of unit quantity of a given final product.

4.16 RULE 10 - TRANSFER OF CREDIT

- (1) If a manufacturer of the final products shifts his factory to another site or the factory is transferred on account of change in ownership or on account of sale, merger, amalgamation, lease or transfer of the factory to a joint venture with the specific provision for transfer of liabilities of such factory, then, the manufacturer shall be allowed to transfer the Cenvat credit lying unutilized in his accounts to such transferred, sold, merged, leased or amalgamated factory.
- (2) If a provider of output service shifts or transfers his business on account of change in ownership or on account of sale, merger, amalgamation, lease or transfer of the business to a joint venture with the specific provision for transfer of liabilities of such business, then, the provider of output service shall be allowed to transfer the Cenvat credit lying unutilized in his accounts to such transferred, sold, merged, leased or amalgamated business.

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- (3) The transfer of the Cenvat credit under sub-rules (1) and (2) shall be allowed only if the stock of inputs as such or in process, or the capital goods is also transferred along with the factory or business premises to the new site or ownership and the inputs, or capital goods, on which credit has been availed of are duly accounted for to the satisfaction of the Deputy Commissioner of Central Excise or, as the case may be, the Assistant Commissioner of Central Excise.

4.17 RULE 11 - TRANSITIONAL PROVISIONS

Sub-rule (1) is a transitional provision which allows credit earned under Cenvat Credit Rules, 2002 and Service tax Credit Rules, 2002 remaining unutilized as on 10.09.2004 to be used under the new Cenvat Credit Rules 2004.

Sub-rule (2) specifically provides that whenever the manufacturer opts out of Cenvat and opts for exemption based on value of clearances, he shall pay the amount equivalent to the Cenvat credit allowed to him in respect of the inputs lying in stock or in process or contained in final products lying in stock and the balance, if any, would lapse.

Sub-rule (3) provides that a manufacturer shall be required to pay an amount equivalent to the CENVAT credit in respect of inputs received for use in the manufacture of the final product which is lying in stock or in process or is contained in the final product lying in stock, if,-

- (i) he opts for exemption from whole of the excise duty leviable on the said final product under a notification issued under section 5A of the Central Excise Act; or
- (ii) the said final product has been exempted absolutely under section 5A of the Act.

If after deducting the said amount from the balance of CENVAT credit (if any lying in his credit) there still remains a balance, it shall lapse. Such balance shall not be allowed to be utilized for payment of duty on any other final product whether cleared for home consumption or for export, or for payment of service tax on any output service, whether provided in India or exported.

Similar is the situation in respect of cases wherein taxable services become exempted. Sub-rule (4) provides that a output service provider shall be required to pay an amount equivalent to the CENVAT credit, if any, taken by him in respect of inputs received for providing the said service and is lying in stock or is contained in the taxable service pending to be provided, when he opts for exemption from payment of whole of the service tax leviable on such taxable service.

After deducting the said amount from the balance of CENVAT credit (if any lying in his credit) if there still remains a balance, it shall lapse. Such balance shall not be allowed to be utilized for payment of duty on any excisable goods, whether cleared for home consumption or for export or for payment of service tax on any other output service, whether

provided in India or exported.

It should be noted that in this case reversal of credit of input services is not required.

4.18 RULE 12 - SPECIAL DISPENSATION IN RESPECT OF INPUTS MANUFACTURED IN FACTORIES LOCATED IN SPECIFIED AREAS OF NORTH EAST REGION, KUTCH DISTRICT OF GUJARAT, STATE OF JAMMU AND KASHMIR AND STATE OF SIKKIM

Notification 32/99 CE and 33/99 CE both dated 8.7.99 have granted exemptions from excise duty for encouraging development of North Eastern India. Notification no. 39/2001 CE dated 31.7.2001 has granted exemption to units located in Kutch district of Gujarat to resurrect the industry post the Gujarat earthquake. Similarly, Notifications No. 56/2002 C.E. 57/2002 C.E. both dated 14.11.2002 and Notifications No. 56/2003 C.E. dated 25.06.2003 and 71/2003 C.E. dated 9.07.2003 have granted exemption to units located in the State of Jammu and Kashmir and Sikkim respectively. Notification No. 20/2007 CE dated 25.04.2007 grants exemption to certain specified goods cleared from a unit located in the States of Assam or Tripura or Meghalaya or Mizoram or Manipur or Nagaland or Arunachal Pradesh or Sikkim from so much of the duty of excise leviable thereon as is equivalent to the amount of duty paid by the manufacturer of goods other than the amount of duty paid by utilization of CENVAT credit under the CENVAT Credit Rules, 2004.

Rule 12 provides that the CENVAT credit on inputs or capital goods cleared under the above notifications shall be admissible as if no portion of the duty paid on such inputs or capital goods was exempted under any of the said notifications. Thus, rule 12 hereby encourages persons in other parts of India to buy inputs and capital goods from such regions, as inputs and capital goods procured from such regions would be deemed to be duty paid.

4.19 RULE 12A – PROCEDURES AND FACILITIES FOR THE LARGE TAX PAYER

- (1) A large taxpayer may remove inputs (except motor spirit, commonly known as petrol, high speed diesel and light diesel oil) or capital goods, as such, on which CENVAT credit has been taken without payment of an amount specified in rule 3(5) of the CENVAT Credit Rules, 2004 under the cover of a transfer challan or invoice from any of his registered premises (sender premises) to his other registered premises (recipient premises) other than a premises of a first or second stage dealer for further use in the manufacture or production of final products in the recipient premises. Such removal shall be subject to the conditions that-
 - (a) the final products are manufactured or produced using the said inputs and cleared on payment of appropriate duties of excise leviable thereon within a period of 6 months, from the date of receipt of the inputs in the recipient premises; or

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- (b) the final products are manufactured or produced using the said inputs and exported out of India, under bond or letter of undertaking within a period of 6 months, from the date of receipt of the inputs in the recipient premises,

and that any other conditions prescribed by the Commissioner of Central Excise, Large Taxpayer Unit in this regard are satisfied.

The transfer challan or invoice shall be serially numbered and shall contain the registration number, name, address of the large taxpayer, description, classification, time and date of removal, mode of transport and vehicle registration number, quantity of the goods and registration number and name of the consignee.

However, if the final products manufactured or produced using the said inputs are not cleared on payment of appropriate duties of excise leviable thereon or are not exported out of India within the said period of 6 months from the date of receipt of the input goods in the recipient premises, or such inputs are cleared as such from the recipient premises, an amount equal to the credit taken in respect of such inputs by the sender premises shall be paid by the recipient premises with interest in the manner and rate specified under rule 14 of these rules. The first recipient premises may take CENVAT credit of such amount paid by it as if it was a duty paid by the sender premises who removed such goods on the basis of a document showing payment of such duties.

Also, if such capital goods are used exclusively in the manufacture of exempted goods, or such capital goods are cleared as such from the recipient premises, an amount equal to the credit taken in respect of such capital goods by the sender premises shall be paid by the recipient premises with interest in the manner and rate specified under rule 14 of these rules.

If a large taxpayer fails to pay any of such amount, it shall be recovered along with interest in the manner as provided under rule 14 of these rules.

It may be noted that the provisions of this sub-rule shall not be applicable if the recipient premises is availing following notifications:

- (i) No. 32/99-CE dated 08.07.1999;
- (ii) No. 33/99-CE dated 08.07.1999;
- (iii) No. 39/2001-CE dated 31.07.2001;
- (iv) No. 56/2002-CE dated 14.11.2002;
- (v) No. 57/2002-CE dated 14.11.2002;
- (vi) No. 56/2003-CE dated 25.06.2003; and
- (vii) No. 71/2003-CE dated 09.09.2003

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(viii) No. 20/2007 CE dated 25.04.2007

Also, the provisions of this sub-rule shall not apply in respect of an EOU or a unit located in a EHTP or STP.

- (2) CENVAT credit of the specified duties taken by a sender premises shall not be denied or varied in respect of any inputs or capital goods, removed as such under sub-rule (1) on the ground that the said inputs or the capital goods have been
- (i) removed without payment of an amount specified in rule 3(5) of these rules; or
 - (ii) used in the manufacture of any intermediate goods removed without payment of duty under sub-rule (1) of rule 12BB of Central Excise Rules, 2002.

For the purpose of this sub-rule intermediate goods shall have the same meaning assigned to it in sub-rule (1) of rule 12BB of the Central Excise Rules, 2002.

- (3) A large taxpayer may transfer CENVAT credit available with one of its registered manufacturing premises or premises providing taxable service to its other registered premises by,-
- (i) making an entry for such transfer in the records maintained under rule 9;
 - (ii) issuing a transfer challan containing registration number, name and address of the registered premises transferring the credit as well as receiving such credit, the amount of credit transferred and the particulars of such entry as mentioned in clause (i),

and such recipient premises can take CENVAT credit on the basis of such transfer challan as mentioned in clause (ii):

It may be noted that such transfer or utilisation of CENVAT credit shall be subject to the limitations prescribed under rule 3(7)(b).

It may be noted that the provisions of this sub-rule shall not be applicable if the registered manufacturing premises is availing following notifications:

- (i) No. 32/99-CE, dated 08.07.1999;
 - (ii) No. 33/99-CE, dated 08.07.1999;
 - (iii) No. 39/2001-CE, dated 31.07.2001;
 - (iv) No. 56/2002-CE, dated 14.11.2002;
 - (v) No. 57/2002-CE, dated 14.11.2002;
 - (vi) No. 56/2003-CE, dated 25.06.2003; and
 - (vii) No. 71/2003-CE, dated 09.09.2003
- (viii) No. 20/2007 CE dated 25.04.2007*

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- (4) A large taxpayer shall submit a monthly return, as prescribed under these rules, for each of the registered premises.
- (5) Any notice issued but not adjudged by any of the Central Excise Officer immediately before the date of grant of acceptance by the Chief Commissioner of Central Excise, Large Taxpayer Unit, shall be deemed to have been issued by Central Excise Officers of the said Unit.
- (6) Provisions of these rules, in so far as they are not inconsistent with the provisions of this rule shall mutatis mutandis apply in case of a large taxpayer.

4.20 RULE 12AA - POWER TO IMPOSE RESTRICTIONS IN CERTAIN TYPES OF CASES

Rule 12AA empowers the Central Government to provide for certain measures including restrictions on a manufacturer, first stage and second stage dealer or an exporter if there is a misuse of CENVAT credit. The Central Government can exercise such powers where having regard to the extent of misuse of CENVAT credit, nature and type of such misuse and any other relevant factors, it is of the opinion that in order to prevent the misuse of the provisions of CENVAT credit, it is necessary in the public interest to impose restrictions. The nature of restrictions, (e.g. restrictions on utilization of CENVAT credit and suspension of registration in case of a dealer) types of facilities to be withdrawn and procedure for issue of such order by an officer authorized by the Board may be specified by a notification in the Official Gazette. The provisions of this rule shall not be subject to anything contained in CENVAT Credit Rules, 2004.

4.21 RULE 13 – POWER OF CENTRAL GOVERNMENT TO NOTIFY GOODS FOR DEEMED CENVAT CREDIT

This Rule seeks to empower the Government to declare vide notifications certain input or input service on which the excise duty, additional duty of customs or service tax paid shall be deemed to have been paid at a rate or equivalent to such amount as may be mentioned in the notification. Cenvat credit shall be allowed on such inputs or input services even if such input or input services are not used directly by the manufacturer of final products or by the provider of taxable service but are contained in the final products or used in providing taxable service.

4.22 RULE 14 - RECOVERY OF CENVAT CREDIT WRONGLY TAKEN OR ERRONEOUSLY REFUNDED

This rule allows for recovery of Cenvat credit taken or utilised wrongly or erroneously refunded along with interest from the manufacturer as provided for in sections 11A and 11AB of the Central Excise Act, 1944 or sections 73 and 75 of the Finance Act.

4.23 RULE 15 - CONFISCATION AND PENALTY

Sub-rule (1) provides that if any person takes Cenvat credit in respect of inputs or capital goods, wrongly or in contravention of any of the provisions of these rules in respect of any inputs or capital goods, then all such goods shall be liable to confiscation and such person shall be liable to a penalty not exceeding the duty on the excisable goods in respect of which any contravention has been committed, or Rs.2,000, whichever is greater.

Sub-rule (2) provides that in a case, where the Cenvat credit has been taken or utilized wrongly on account of fraud, willful mis-statement, collusion or suppression of facts, or contravention of any of the provisions of the Act or the rules made thereunder with intention to evade payment of duty, then, the manufacturer shall also be liable to pay penalty in terms of the provisions of section 11AC of the Act.

Sub-rule (3) lays down that a person shall be liable to a penalty if he takes Cenvat credit in respect of input services, wrongly. Further, contravention of any of the provisions of these rules in respect of any input service shall also be liable to be penalized. The penalty may extend to an amount not exceeding Rs.2,000.

Sub-rule (4) provides that in a case, where the CENVAT credit in respect of input services has been taken or utilized wrongly by reason of fraud, collusion, willful mis-statement, suppression of facts, or contravention of any of the provisions of the Finance Act or of the rules made thereunder with intention to evade payment of service tax, then, the provider of output service shall also be liable to pay penalty in terms of the provisions of section 78 of the Finance Act.

Sub rule (5) provides that any order under sub-rule (1), sub-rule (2), sub-rule (3) or sub-rule (4) shall be issued by the Central Excise Officer following the principles of natural justice.

4.24 RULE 15A – GENERAL PENALTY

This rule provides for general penalty upto Rs.5000/- in case of contravention of any of the provisions of the CENVAT Credit Rules, 2004, for which no specific penal provision exists.

4.25 RULE 16 - SUPPLEMENTARY PROVISION

Any notification, circular, instruction, standing order, trade notice or other order issued under Cenvat Credit Rules, 2002 or the Service Tax Credit Rules, 2002, by the Board, Chief Commissioner or Commissioner of Central Excise and in force at the commencement of these rules shall, to the extent it is relevant and consistent with these rules be deemed to be valid.

References in any rule, notification, circular, instruction, standing order, trade notice or other order to the Cenvat Credit Rules, 2002 and any provision thereof or, as the case be, the Service Tax Credit Rules, 2002 and any provision thereof shall, on the commencement of these rules, be construed as references to the Cenvat Credit Rules, 2004 and any corresponding provision thereof.

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4.26 CENVAT CREDIT NEED NOT BE REVERSED WHERE THE MANUFACTURING PROCESS IS HELD AS NOT CHARGEABLE TO EXCISE DUTY BY THE COURTS [SECTION 5B]

Sometimes it happens that a process undertaken by a manufacturer is held as not chargeable to excise duty by the Courts, though the assessee has been availing credit of excise duty/service tax/cess paid on the inputs/capital goods/input services used in manufacturing the final product and paying excise duty on such final products.

Section 5B of the Central Excise Act, 1944 provides that in such cases the Central Government may order for non-reversal of the credit allowed to the assessee by issuing a notification. The notification may specify the conditions subject to which such non-reversal of credit may be ordered. Further, the Central Government may also order for non-reversal of credit, if any, taken by the buyer of the said product in such notification.

It may be noted that such non-reversal of the credit shall not be ordered if the assessee has preferred a claim for refund of excise duty paid by him.

4.27 CENVAT AND ASSESSABLE VALUE

In case of *CCE v. Dai Ichi Karkaria Ltd.* - 1999 (112) E.L.T. 353, the Supreme Court has held that since modvat (now Cenvat) element is not reckoned as a cost of the raw materials by a man of commerce, the question of including the same in the assessable value of the final product does not arise.

4.28 CENVAT ON DEFECTIVE GOODS RETURNED

In *CCE v. Tin Manufacturing Co* -2000 (119) E.L.T. 290 (T-LB) the Large Bench of the Tribunal held that so long as the defective goods were specified and were duty paid, they would become inputs since they would have to be remade. Now this concept has been brought in under rule 16 of Central Excise Rules, 2002 giving benefit of the Cenvat credit on the goods returned for repair, reprocessing, remaking or for any other purpose.

4.29 BALANCE OF CENVAT CREDIT LYING UNUTILIZED AT YEAR END

It should be kept in mind that if such unutilised credit has been claimed as expenditure for the year, the same should be written off in the Balance Sheet. It should not be used subsequently for the purpose of payment of duty.

Self-examination questions

1. What are the duties in respect of which CENVAT credit can be availed under the CENVAT Credit Rules, 2002?
2. Discuss the provisions prescribed in CENVAT Credit Rules, 2004 for a situation where an output service provider renders both taxable as well as exempted output

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services by using common inputs/input services and maintains only one set of books of accounts for taxable and exempted services.

3. Discuss the provisions relating to information on principal inputs in context of CENVAT Credit Rules, 2004.
4. Can credit be taken only after making payment against the bill/invoice/challan? Discuss.
5. Who is an “input service distributor”?
6. Credit for inputs is not available if the final products are exempted goods. What are the exceptions to this rule?
7. A machine was received in a factory at 5 p.m. on 31.03.2009. It was not erected at that time. The machine was meant for the manufacture of dutiable as well as zero duty goods. The assessee decided to claim depreciation under section 32 of Income-tax Act on the sans duty price of machinery. Can the manufacturer take CENVAT Credit? If yes, what is the amount of credit that he can avail?
8. India Cements Ltd. is engaged in the business of manufacturing cement. For this purpose, limestone is excavated from a mine, which is situated at a distance of few kilometres from the plant where the cement is manufactured. The mine is connected to the main plant through a ropeway. Explosives are used for blasting the mine to excavate limestone. Can CENVAT credit be taken on such explosives? Discuss.
9. Answer the following with reference to CENVAT Credit Rules, 2004:
 - (a) ‘A’ manufactures a certain final product in which petrol is used among other inputs. Can he avail CENVAT credit on petrol?
 - (b) ‘B’ is an outdoor caterer. He has purchased a lorry for carrying utensils, tables, groceries, vegetables etc. to the place of service. Can ‘B’ avail credit of the excise duty paid by him on the purchase of the lorry?
 - (c) Can a manufacturer located in Jammu utilize the credit of service tax availed on input services received in New Delhi for payment of excise duty on his final products cleared in Jammu?
 - (d) Inputs are received in the factory of the manufacturer on 10.11.2009 but are issued for the production process on 10.12.2009. When should the manufacturer avail credit?
10. With reference to CENVAT Credit Rules, 2004, discuss giving reasons whether the following statements are true or false:
 - (a) Motor vehicles are eligible capital goods both for manufacturers and all output service providers.

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- (b) An input service distributor has to furnish a half yearly statement in the form specified by the Board to the jurisdictional Superintendent of Central Excise.
- (c) Cenvat credit shall be allowed on inputs which are sent to the job worker for the manufacture of intermediate goods necessary for the manufacture of final products, if they are received back in the factory within 180 days of their being sent to the job worker.
- (d) Where the capital goods are cleared as waste and scrap, the manufacturer has to pay an amount equal to the duty leviable on transaction value. Such amount paid can be availed as CENVAT credit.
- (e) Credit of basic excise duty can be utilized for payment of education cess whereas the *vice versa* is not possible.

Answers

7. As per Rule 4 of CENVAT Credit Rules, 2002 CENVAT credit on capital goods can be availed on the following propositions--:

- (1) The capital goods should have been actually received in the factory (Physical receipt is a must, as in the case of inputs. Erection of the machinery is not compulsory for the first year).
- (2) The capital goods might have been received at any point of time in a financial year.
- (3) Not more than 50% of the duty paid on the capital goods in the same financial year can be taken as CENVAT credit. Credit for the balance can be taken in any subsequent year, provided the goods are in the possession and use of manufacturer.
- (4) Capital goods must not be used exclusively in the manufacture of exempted goods.
- (5) Depreciation under section 32 of the Income tax Act on the part of the value of the capital goods that represents excise duty cannot be claimed, if the manufacturer avails CENVAT credit.

As all the conditions specified above are fulfilled in the given case, 50% of the duty paid by the manufacturer can be availed as CENVAT credit in the first year and the balance in any subsequent year, if the machine remains to be in his possession and use.

8. The Supreme Court in the case of *Vikram Cement v. CCE*. (2006) 194 ELT 3 (SC) has held that CENVAT credit on inputs being explosives used for blasting mines to produce limestone for use in manufacture of cement/clinkers in factory situated at some distance away from mines could not be denied on the ground that they were not used as inputs within the factory.

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Note: The above-mentioned decision overrules the contrary opinion of the Supreme Court in the case of *J.K. Udaipur Udyog Ltd. 2004 (171) E.L.T. 289 (SC)*. In this case, the credit on explosives used for blasting mines was disallowed on the ground that the same were not used within the factory but in a mine which could not qualify to be a factory.

Further, it may be noted that in *Vikram Cement v. CCE 2006 (197) ELT 145 (SC)*, it has been held that CENVAT credit is available only when mines are captive mines i.e. they constitute one integrated unit with the main cement factory. Credit would not be available if the supplies from the mine are made to various cement factories of different assesseees.

9. (a) No. Petrol (motor spirit) is specifically excluded from the list of eligible inputs under Rule 2(k).
- (b) Yes. As per Rule 2(a) motor vehicles are treated as capital goods in the case of an outdoor caterer.
- (c) No. Cenvat Credit Rules, 2004 in relation to availment and utilization of service tax credit are not applicable in the State of Jammu and Kashmir, as service tax law does not apply in Jammu and Kashmir.
- (d) Credit can be availed on 10.11.2009 immediately on receipt of the inputs in the factory of the manufacturer [Rule 4(1)].
10. (a) False. Rule 2(a) defines capital goods to mean
- (A) the following goods, namely:-
- (i) all goods falling under Chapter 82, Chapter 84, Chapter 85, Chapter 90, heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804 of the First Schedule to the Excise Tariff Act;
 - (ii) pollution control equipment;
 - (iii) components, spares and accessories of the goods specified at (i) and (ii);
 - (iv) moulds and dies, jigs and fixtures;
 - (v) refractories and refractory materials;
 - (vi) tubes and pipes and fittings thereof; and
 - (vii) storage tank,
- used-
- (1) in the factory of the manufacturer of the final products, but does not include any equipment or appliance used in an office; or

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(2) for providing output service;

- (B) motor vehicle registered in the name of provider of output service for providing taxable service as specified in sub-clauses (f), (n), (o), (zr), (zpz), (zzt) and (zzw) of clause (105) of section 65 of the Finance Act.

Motor Vehicles fall under Chapter 87. Thus, the manufacturers cannot avail credit on motor vehicles. However, in case of taxable services credit on motor vehicles can be availed in case of abovementioned specific output services. These services are:

- (1) Courier services
 - (2) Tour operator's services
 - (3) Rent-a-cab scheme operator's services
 - (4) Cargo handling agency's services
 - (5) Goods transport agency's services
 - (6) Outdoor caterer's services
 - (7) Pandal or shamiana contractor's services
- (b) False. The sub-rule 10 of rule 9 provides that the input service distributor shall furnish a half yearly **return** in the form specified by the Board to the jurisdictional Superintendent of Central Excise.
- (c) True. Rule 4(5) lays down that CENVAT credit shall be allowed on goods (being inputs or capital goods) sent to the job worker for further processing, testing, repair, reconditioning or for the manufacture of intermediate goods necessary for the manufacture of final products or any other purpose, if they are received back in the factory within 180 days of their being sent to the job worker. In case they are not returned within 180 days the credit on such goods has to be reversed. However, credit can be retaken once the goods come back.
- (d) True. Sub-rule (5A) of rule 3 provides that if the capital goods are cleared as waste and scrap, the manufacturer shall pay an amount equal to the duty leviable on transaction value. Rule 3(6) provides that the amount paid under sub-rule (5A) shall also be eligible as CENVAT credit as if it was duty paid by the person who removed such goods under sub-rule (5A).
- (e) True. As per rule 3(4) read with rule 3(1) and rule 3(7)(b), the Cenvat credit of basic excise duty, special excise duty, service tax and AED(GSI) can be utilised for payment of **any** duty or service tax as credit of all duties together is known as 'Cenvat credit'. Hence, credit of basic excise duty can be utilised for payment of education cess on excisable goods. However, as per rule 3(7)(b), credit of education cess paid on excisable goods can be utilised only for payment of education cess on excisable goods or taxable services.