Write Up on Input Service tax : Budget 2011-12:

Input Service

Cenvat Credit is available on input goods, input services and capital goods. Manufacturer as well as service provider will be eligible to get Cenvat credit of 'input services'.

Definition of 'input service' has been changed w.e.f. 1-4-2011. The new definition is significantly different from the earlier definition of 'input service'. Rule 2(l) of Cenvat Credit Rules (as effective from 1-4-2011), defines 'input service' as follows –

"Input service" means any service, -

(i) used by a provider of taxable service for providing an output service; or

(ii) used by a 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 modernisation, 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, accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry, security, business exhibition, legal services, inward transportation of inputs or capital goods and outward transportation upto the place of removal;

but excludes services

(A) specified in sub-clauses (p), (zn), (zzl), (zzm), (zzq), (zzzh) and (zzzza) of clause (105) of section 65 of the Finance Act (hereinafter referred as specified services), in so far as they are used for- (a) construction of a building or a civil structure or a part thereof; or (b) laying of foundation or making of structures for support of capital goods, ***except*** for the provision of one or more of the specified services; or

(B) specified in sub-clauses (d), (o), (zo) and (zzzzj) of clause (105) of section 65 of the Finance Act, in so far as they relate to a motor vehicle ***except*** when used for the provision of taxable services for which the credit on motor vehicle is available as capital goods; or

(C) such as those provided in relation to outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, membership of a club, health and fitness centre, life insurance, health insurance and travel benefits extended to employees on vacation such as Leave or Home Travel Concession, ***when such services are used primarily for personal use or consumption of any employee.***

Certain services like outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, membership of a club, health and fitness centre, life insurance, health insurance and travel benefits extended to employees on vacation such as Leave or Home Travel Concession have been specifically excluded. However, this exclusion is ***only when*** such services are used primarily for personal use or consumption of any employee. This exclusion will not apply in other cases. For example, outdoor catering for 'sales promotion' would be eligible. Club membership fee of a director (who is not employee) would be eligible.

Background of Input Service Tax:-

Cenvat credit is not available if inputs or input services are used for manufacture of exempted goods or provision of exempted output services.

As per Rule 6(1) of Cenvat Credit Rules, Cenvat credit is not admissible on such quantity of input or input service which is used in manufacture of exempted goods or provision of exempted services. Thus, if inputs and input services are partly used in exempted final product/output service, Cenvat credit of that portion of input/input service will not be available.

Partial manufacture/provision of exempted products/services – Cenvat credit of inputs and input services is not available if final product/output service is exempt from excise duty/service tax. In case of manufacturer manufacturing both exempt and dutiable goods (or service provider providing taxable as well as exempt services), it may happen that same inputs/input services are used partly for manufacture of dutiable goods/taxable services and partly for exempted goods/services.

In such cases, the manufacturer/service provider has following four options w.e.f. 1-4-2011 –

(a) Maintain separate inventory and accounts of receipt and use of inputs and input services used for exempted goods/exempted output services – Rule 6(2) of Cenvat Credit Rules

(b) Pay amount equal to 5% of value of exempted goods (if he is 'manufacturer) and of value of exempted services (if he is service provider) – Rule 6(3)(i) [The 'amount' payable was 6% of value of exempted services during the period 7-9-2009 to 31-3-2011].

(c) Pay an 'amount' equal to proportionate Cenvat credit attributable to exempted final product/ exempted output services, as provided in rule 6(3A) – Rule 6(3)(ii) of Cenvat Credit Rules

(d) Maintain separate accounts for inputs and pay 'amount' as determined under rule 6(3A) in respect of input services - – Rule 6(3)(iii) of Cenvat Credit Rules as inserted w.e.f. 1-4-2011.

A: Provisions relating to option

Option has to be exercised in respect of all exempted goods manufactured and all exempted output services provided. The option once exercised shall not be changed in remaining part of financial year.

B: *Option is to person availing Cenvat credit*

Rule 6(3) uses the words 'if manufacturer or provider of output service opts not to maintain separate accounts'. Thus, whether to maintain separate accounts or not is at the option of person availing Cenvat credit. He cannot be compelled to maintain or not maintain separate accounts.

<u>Procedures explained in detail:-</u>

1. **Maintaining Separate Accounts of Input and Input Services:**

1-1 Rule 6(2) of Cenvat Credit Rules as recast w.e.f. 1-4-2011 elaborates how records in respect of exempted goods ad exempted services shall be maintained.

(a) the receipt, consumption and inventory of inputs used- (i) in or in relation to the manufacture of exempted goods; (ii) in or in relation to the manufacture of dutiable final products excluding exempted goods; (iii) for the provision of exempted services; (iv) for the provision of output services excluding exempted services.

Assessee shall take CENVAT credit only on inputs under sub-clauses (ii) and (iv) of clause (a).

(b) the receipt and use of input services- (i) in or in relation to the manufacture of exempted goods and their clearance upto the place of removal; (ii) in or in relation to the manufacture of dutiable final products, excluding exempted goods, and their clearance upto the place of removal; (iii) for the provision of exempted services; and (iv) for the provision of output services excluding exempted services,

Assessee shall take CENVAT credit only on input services under sub-clauses (ii) and (iv) of clause (b).

2. **Payment of 'amount' on exempted final product/exempt services**

Assessee can opt to pay 'amount' of **5%** of 'value of exempted final product or 'value of exempted services [rule 6(3)(i)].

Education cess not payable - Education cess and SAH education cess is payable only on 'duties of excise'. 'Amount' is not 'duty'. Hence, education cess and SAH education cess is not payable on such 'amount'.

3. **Proportionate reversal of Cenvat Credit**

If assessee intends to pay 'amount' on proportionate basis (and not at flat rate of 5% on exempted goods and services), he has following two options w.e.f. 1-4-2011.

(a) Pay an 'amount' equal to proportionate Cenvat credit attributable to exempted final product/ exempted output services, as provided in rule 6(3A) – Rule 6(3)(ii) of Cenvat Credit Rules

(b) Maintain separate accounts for inputs and pay 'amount' as determined under rule 6(3A) in respect of input services - – Rule 6(3)(iii) of Cenvat Credit Rules as inserted w.e.f. 1-4-2011.

The option (b) above was not available upto 31-3-2011.He has to pay 'amount' provisionally on monthly basis, At the year end, he has to calculate exact amount and ay difference if any or adjust excess paid.

3-1 *Inform option to Superintendent*

The assessee should inform following details to Superintendent, while exercising the option of proportionate reversal [Rule 6(3A)(a)] -

- name, address and registration No. of the manufacturer of goods or provider of output service.
- date from which the option under this clause is exercised or proposed to be exercised.
- description of dutiable goods or taxable services.
- description of exempted goods or exempted services.
- CENVAT credit of inputs and input services lying in balance as on the date of exercising the option under this condition.

Such option has to be exercised in respect of all exempted goods manufactured and all exempted output services provided. The option once exercised shall not be changed in remaining part of financial year – *Explanation* I to Rule 6(3) inserted w.e.f. 1-4-2008.

If assessee intends to pay 5% 'amount' on exempted final products/exempted final services, such intimation is not required.

3-2 Mode of calculations of proportionate reversal

The mode of calculation is as follows –

Assessee should first take entire Cenvat credit of inputs and input services used in exempted as well as taxable final products and exempted as well as taxable services.

Calculation of amount to be reversed - At the end of month, assessee should calculate Cenvat credit attributable to exempted final products and exempted services on provisional basis, as follows –

Amount to be reversed at end of month		
(1)	Rule 6(3A)(b)(i)	Inputs used for exempted final products
(2)	Rule 6(3A)(b)(ii)	Inputs used for exempted services (On proportionate basis, based on ratio of previous year)
(3)	Rule 6(3A)(b)(iii)	Input services used for exempted final products and exempted services (On proportionate basis based on ratio of previous year).
	Total	1+2+3 = amount to be reversed every month on provisional basis

Calculations at the end of the year - At end of the year, assessee should calculate the ratios on actual basis and make fresh calculations and pay difference, if any, before 30th June. If it is found that he had paid excess amount based on provisional ratio, he can adjust the difference himself by taking credit.

4 Calculation of 'value' for purposes of rule 6(3) and 6(3A):-

As per *Explanation* I to Rule 6(3D) inserted w.e.f. 1-4-2011, "Value" for the purpose of rules 6(3) and 6(3A) of Cenvat Credit Rules -

(a) shall have the same meaning as assigned to it under section 67 of the Finance Act, read with rules made there under or, as the case may be, the value determined under section 3, 4 or 4A of the Excise Act, read with rules made thereunder.

(b) in the case of a taxable service, when the option available under sub-rules (7), (7B) or (7C) of rule 6 of the Service Tax Rules, 1994, or the Works Contract (Composition Scheme for payment of Service Tax) Rules, 2007 has been availed, shall be the value on which the rate of service tax under section 66 of the Finance Act, read with an exemption notification, if any, relating to such rate, when applied for calculation of service tax results in the same amount of tax as calculated under the option availed; or

(c) in case of trading, shall be the difference between the sale price and the purchase price of the goods traded.