



1,000. Education Cess – As applicable. During the month, he received various inputs on which total duty paid by suppliers of inputs was as follows – Basic duty – Rs 40,000, Education Cess – Rs 800, SAH education Cess - Rs 400. Service tax paid on input services was as follows – Service Tax – Rs 8,000. Education cess – Rs 160, SAH education Cess - Rs 80. How much duty the assessee will be required to pay by GAR-7 challan for the month of July 2007, if there was no opening balance in his PLA account?

Kept for self study.

4.9 DOCUMENTS FOR AVAILING CENVAT CREDIT

Rule 9(1) of Cenvat Credit Rules prescribes that Cenvat Credit can be taken on the basis of -

- Invoice of manufacturer from factory
- Invoice of manufacturer from his depot or premises of consignment agent
- Invoice issued by registered importer
- Invoice issued by importer from his premises or consignment registered with Central Excise
- Invoice issued by registered first stage or second stage dealer
- Supplementary Invoice by manufacturer
- Bill of Entry
- Certificate issued by an appraiser of customs in respect of goods imported through foreign post office
- TR-6 or GAR-7 Challan of payment of tax where service tax is payable by other than input service provider
- Invoice, bill or challan issued by provider of input service on or after 10-9-2004
- Invoice, Bill or Challan issued by input service distributor under rule 4A of Service Tax Rules.

Credit in case of defects in duty paying document only with permission of AC/DC – Cenvat credit is available on basis of proof of duty paying document like Invoice or Bill of Entry. Sometimes, there are some minor defects in the duty paying document, which are technical in nature. However, fact of duty payment is not in doubt.

Rule 9(2) as amended w.e.f. 1-3-2007 provides that Cenvat credit can be taken only if **all** the particulars as prescribed in Central Excise Rules, 2002 or Service Tax Rules, 1994 are contained in the eligible duty paying document.

As per *proviso* to rule 9(2), if all prescribed details are not available in duty paying document, at least following minimum details should be available - (a) Details of duty or service tax payable

(b) description of goods or taxable service (c) assessable value (d) Central Excise or Service Tax Registration Number and (e) name and address of the factory or warehouse or premises of first or second stage dealers or provider of taxable service.

If all prescribed details are not available in duty paying document (but minimum details as prescribed above are available) and if Jurisdictional Assistant / Deputy Commissioner is satisfied that such goods or services covered by the document have been received and accounted for in books of account of receiver, he may allow Cenvat credit.

Thus, even if there is minor defect or omission in duty paying document, the assessee will have to make application to AC/DC and seek his permission to avail Cenvat credit

Provisions when dealer of imported goods is claiming refund of Special CVD of Customs – A dealer who imports goods and sales them in India after paying Vat / sales tax can claim refund of special CVD of 4% paid u/s 3(5) of Customs Tariff Act, as per Notification No. 102/2007-Cus dated 14-9-2007. If he intends to claim refund, he is required to make mention in his invoice to buyer that no credit of such additional duty shall be admissible (to buyer).

If a first stage or second stage dealer receives goods under an invoice which mentions that Cenvat credit of the special CVD paid u/s 3(5) of Customs Tariff Act is not admissible, he should make similar endorsement in his invoice to buyer. – *proviso* to rule 11(7) of Central Excise Rules. If such remark is there, the buyer cannot avail Cenvat credit of such special CVD *proviso* to rule 9(1) inserted w.e.f. 14-9-2007.

4.10 EXEMPTED GOODS/OUTPUT SERVICES

- Cenvat credit is available only if final product is dutiable.
- If assessee is manufacturing exempted as well as dutiable goods in same factory, he should maintain separate records.
- If common inputs/input services are utilised for exempted as well as taxable final product, assessee is required to pay 10% 'amount' on exempted final product.
- In case of services, his utilisation of credit is restricted to 20% of tax payable on taxable services.

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 three options (w.e.f. 1-4-2008) –

- (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 10% of value of exempted goods (if he is 'manufacturer) and / or 8% of value of exempted services (if he is service provider) if he does not maintain separate inventory and records – Rule 6(3)(i) w.e.f. 1-4-2008.
- (c) Pay an 'amount' equal to proportionate Cenvat credit attributable to exempted final product/ exempted output services – Rule 6(3)(ii) w.e.f. 1-4-2008.

Cenvat credit on capital goods – If capital goods are partly used for exempted goods and partly for dutiable final products, entire Cenvat credit of duty paid on capital goods is available. Cenvat credit of duty on capital goods is not allowable only when it is *exclusively* used for manufacture of final products [rule 6(4)]

No reversal or payment of amount in certain cases – If excisable goods are removed to SEZ, EOU, EHTP, STP, UN agencies or for exports or removal of gold or silver arising in manufacture of copper or zinc by smelting, payment of 10% 'amount' is not required [rule 6(6)].

Cenvat credit of service tax in case of supplies made by DTA to EOU - Supplies from DTA to EOU are entitled to Cenvat credit of service tax paid – para 6.11(v) of FTP.

4.10.1 Options available to manufacturer manufacturing both dutiable and exempt goods and service provider providing taxable as well as exempt services

The manufacturer/service provider has three options –

Maintain separate inventory and accounts - Maintain separate inventory and accounts of receipt and use of inputs and input services used for exempted goods/exempted output services. In such cases, he should not avail Cenvat credit of the inputs and input services which are used in exempted final services at all – Rule 6(2) of Cenvat Credit Rules.

Pay 10% 'amount' on value of exempted goods or 8% 'amount' on value of exempted services if separate inventory and records not maintained - If the manufacturer/service provider opts not to maintain such separate accounts, he has to pay an amount equal to 10% of the 'value' of such exempted goods or 8% of the value of 'exempted services' [Rule 6(3)(i) w.e.f. 1-4-2008 (Such payment can be made by debit to Cenvat credit account or PLA [*explanation II* to rule 6(3A)].

He cannot utilise Cenvat credit of inputs/input services utilised exclusively for manufacture or exempted final product or exempted output services, as is clarified in Explanation II to rule 6(3) inserted w.e.f. 1-4-2008.

Thus, he cannot utilise Cenvat credit in respect of inputs/input services utilised exclusively for manufacture of exempted final products or exempted taxable services. In addition, he has to pay 10%/8% amount. Thus, the option of payment of 10%/8% amount is not likely to be very attractive in most of the cases.

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.

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

Pay proportionate amount attributable to Cenvat credit utilised for exempted final product/exempted output services – The manufacturer/service provider can opt to pay an 'amount' which is proportional to Cenvat credit availed on exempted final product/exempted output services [rule 6(3)(ii) w.e.f. 1-4-2008]

He cannot utilise Cenvat credit of inputs/input services utilised exclusively for manufacture or exempted final product or exempted output services, as is clarified in Explanation II to rule 6(3) inserted w.e.f. 1-4-2008.

Thus, he cannot utilise Cenvat credit in respect of inputs/input services utilised exclusively for manufacture of exempted final products or exempted taxable services. In addition, he has to pay proportionate amount relating to exempted final products/exempted output services.

This option seems to be much better than payment of 8%/10%.

If he wants to exercise this option, he has to inform details as prescribed in rule 6(3A) of Cenvat Credit Rules to Superintendent of Central Excise.

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.

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

4.10.2 Determination of Cenvat credit attributable to exempted final product/exempted services

If assessee intends to pay amount on proportionate basis, the 'amount' is to be calculated as provided in rule 6(3A) of Cenvat Credit Rules. He has to pay 'amount' provisionally on monthly basis. At the yearend, he has to calculate exact amount and pay difference if any or adjust excess amount paid.

Principle behind the calculations – 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. Then, at the end of month, he should calculate Cenvat credit attributable to exempted final products and exempted services on provisional basis, as follows –

Inputs used for exempted final products (Based on his own Input/Output ratio, even in case of common inputs like consumables etc.) + Inputs used for exempted services (On proportionate basis, based on ratio of previous year) + Input services used for exempted final products and exempted services (On proportionate basis based on ratio of previous year).

This amount should be reversed after end of each month.

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.

In the first year of production or provision of services, ratios of previous year are not available. In that case, the calculations need not be made for the whole year. However, calculations should be made after the year is over and amount attributable to Cenvat credit on exempted final products and exempted services should be calculated and paid.

The basic idea behind the mode of calculations is sound and correct as per Vat principles. However, calculations are not easy and are prone to litigation.

There is no provision to calculate input services used exclusively for exempted services. This has to be done on ratio basis only.

Payment of 'amount' when intermediate product captively consumed in manufacture of another final product – In *CCE v. Texmo Industries* (2007) 213 ELT 615 (CESTAT), assessee used common inputs to manufacture rough castings. Some castings were sold while about 20% castings were captively consumed for manufacture of pumps. The pumps were also exempt from duty. It was held that 10% 'amount' is payable on value of castings and not on value of pumps. 'Casting' is the 'final product' and not 'pumps' – same view in *Texmo Industries v. CCE* (2007) 208 ELT 338 (CESTAT 3 member bench).

4.11 REMOVAL OF INPUT, CAPITAL GOODS AND WASTE

- Inputs and capital goods on which Cenvat credit was taken can be removed 'as such' on payment of 'amount' equal to Cenvat credit availed.
- If capital goods are sold as scrap after use, an 'amount' equal to duty on scrap value is payable.
- Inputs on which Cenvat was availed can be sent outside for job work. These should come back within 180 days.
- Direct despatch from place of job worker can be done with permission.
- Waste is final product for excise purposes and duty is payable as if final product is being cleared.
- If a particular waste is not mentioned in Central Excise tariff, neither any amount nor duty is payable at the time of clearance.

Removal of capital goods after use

Provisions of rule 3(5) apply when inputs or capital goods are removed 'as such'. Rule 2(a)(A) of Cenvat Credit Rules states that capital goods should be 'used'. Duration is not specified. Hence, even if the capital goods are used for one day, Cenvat eligibility of capital goods is established. After use, the capital goods can be removed either as scrap or as second hand capital goods.

Removal of capital goods as waste and scrap – As per rule 3(5A) (inserted w.e.f. 16-5-2005), if capital goods are removed as scrap, the manufacturer shall pay an 'amount' equal to duty payable on transaction value. In other words, an 'amount' equal to duty on scrap value should be paid. It should be

shown as 'amount' in the invoice and not 'duty'. Rule 3(6) makes it clear that the buyer can avail Cenvat credit of the 'amount'.

Removal of capital goods as second hand goods – It is not that manufacturer will remove old capital goods only as scrap. He can as well sell it as second hand capital goods, if he does not need them. The machinery may be in working condition or could be brought in working condition after some expenditure.

In such case, if capital goods are removed after use, the manufacturer or output service provider shall pay an 'amount' (not 'excise duty') equal to 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 [second proviso to rule 3(5) of Cenvat Credit Rules, inserted w.e.f. 13-11-2007].

For example, if capital goods are received in July 2007 (duty paid Rs 1,00,000), 50% i.e. Rs 50,000 credit was taken in November 2007, balance 50% credit was taken in April 2008, capital goods were installed in January 2008 and were sold after use in July 2009, the 'quarters' involved are 8 (2007 – 1, 2008-4, 2009 – 3) for first 50% and 6 for balance 50%.

Thus, assessee can get deduction of 20% of first Rs 50,000 (Rs 10,000) and 15% of balance Rs 50,000 (Rs 7,500). He has to pay 'amount' of Rs 82,500 (1,00,000 – 10,000 – 7,500).

The buyer can avail Cenvat credit of this 'amount' as made clear in rule 3(6) of Cenvat Credit Rules. Hence, seller should clear the second hand capital goods under 'invoice' charging 'amount' in invoice (not excise duty).

H Ltd. purchased a Boring-Drilling machine at a cum-duty price of Rs. 32,14,476. The Excise duty rate charged on the said machine was @ 16% plus education cess of 2% plus SAH education cess of 1%. The machine was purchased on 01.04.2007 and disposed of on 30.09.2008 for a price of Rs. 12 lakhs in working condition as second hand machinery. The company was claiming depreciation @ 25% following Straight Line Method. Using the said information, answer the following questions: (i) What is the Excise duty paid on the machine? (ii) What is the Cenvat credit allowable under Cenvat Rules? (iii) What is the amount of Cenvat credit reversible or duty payable at the time of clearance of the said machinery?.

Cum-duty price Rs. 32,14,476. Hence, Basic Price i.e. Assessable value = $32,14,476 \times 100 / 116.48$ = Rs. 27,59,680.63.

Total duty paid - 4,54,795.37

As per Cenvat Credit Rules, 50% Cenvat credit can be availed in current financial year and balance 50% of Cenvat is allowable only in following financial year, if the capital Goods are in possession and use. Hence, 50% Cenvat credit can be taken on 1-4-2007. Since the Capital goods were in use for six months in the year 2007-08, Cenvat of balance 50% is allowable on 1-4-2008.

As per second proviso to rule 3(5) of Cenvat Credit Rules, if capital goods are removed after use, the manufacturer or output service provider shall pay an 'amount' (not 'excise duty') equal to 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. It is assumed that assessee took

credit on 1-4-2007. Since machinery was disposed of on 30-9-2008, reduction for 6 quarters @ 2.5% per quarter i.e. 15% will be available. Thus, assessee is required to pay 'amount' equal to 85% of Rs 4,54,795.37 i.e. Rs 3,86,576.06.

4.12 OTHER PROVISIONS OF CENVAT

Refund of service tax paid in respect of certain services utilised for exports – A manufacturer exporter can avail Cenvat credit of certain input services utilized in relation to export. However, according to Government press release dated 6-10-2007 – 10 STT 25 (St), press note dated 17-9-2007 – 10 STT 14 (St), press release dated 29-11-2007 – 11 STT 55 (St), some services utilised for exports do not fall within the definition of input services [In my view, they do fall within the definition of 'input service' for a manufacturer. The reason is that exports are invariably on FOB basis and hence port is the 'place of removal'. Another reason is the wide definition of 'input service']. Similarly, a merchant exporter utilises various input services for export of goods which he cannot avail any Cenvat credit. In respect of following such services, an exporter can claim refund of service tax paid on such services, under Notification No. 41/2007-ST dated 6-10-2007.

These services are – (a) General Insurance Services (b) Technical testing and analysis (c) Technical inspection and certification (d) Port and other port (e) Transport of export goods by road or by rail (f) Cleaning activity (g) Storage and warehousing (h) Courier services (i) Transport of goods by road from place of removal (j) Transport of goods by container from place of removal (k) CHA service (l) Banking and financial services (m) Services of commission agent.

(No refund is available in respect of other input services utilised for export)

Transfer of credit of duty paid on material lying at place of job worker permissible - In *CCE v. Vaishali India* (2008) 224 ELT 247 (CESTAT SMB), assessee was shifting factory to new premises and sought permission for transfer of credit of duty paid on inputs lying at the premises of job worker. It was held that such credit cannot be denied.

Cash Refund if Cenvat cannot be utilised by exporter - If the credit cannot be used for payment of duty on any other final goods or service tax on other services, manufacturer or service provider can get cash refund of the same, if final products or output services were exported without payment of duty (either under bond or after giving Letter of undertaking), or if these were used in the intermediate product cleared for export. Refund is not admissible if exporter has availed duty drawback or has claimed rebate of duty in respect of such duties or has claimed rebate of service tax under Export of Service Rules - Rule 5 of Cenvat Credit Rules.

This provision is only for physical exports and not for deemed exports or home clearances.

The rule 5 states that no drawback should be claimed. Actually, duty drawback of customs portion should be allowable, since refund of Cenvat credit is only in respect of excise portion of duty drawback. Unfortunately, the way rule 5 is worded, this does not seem possible.

Para 2.48.1 of Foreign Trade Policy (as amended w.e.f. 7-4-2006), reads as follows, 'For all goods and services which are exported from units in DTA (Domestic Tariff Area) and units in EOU / EHTP / STP / BTP, remission of service tax shall be allowed'.

Para 6.11(c)(v) of Foreign Trade Policy (as amended w.e.f. 7-4-2006) states that EOU/EHTP/STP/BTP units shall be entitled to Cenvat Credit of service tax paid.

Rule 5 of Cenvat Credit Rules has been amended w.e.f. 14-3-2006 to provide for refund of Cenvat credit when final products or output service is exported.

Procedure for claiming refund of service tax paid on input services and excise duty on inputs has been specified in notification No. 5/2006-CE(NT) dated 14-3-2006.

Penalty for violation of Cenvat Credit Rules – Penalty upto Rs 5,000 can be imposed for violation of Cenvat Credit Rules [rule 15A of Cenvat Credit Rules inserted w.e.f. 1-3-2008].

4.13 ACCOUNTING TREATMENT OF INPUTS IN CENVAT

Accounting for Cenvat in books of account of assessee needs following considerations

- (a) Since credit is available of excise duty/service tax paid while obtaining inputs/input services, duty/service tax paid on inputs while purchase is not an expense but an asset.
- (b) Unavailed Cenvat is not available as refund (except when it is a case of exports). This may happen when duty/service tax paid on inputs is more than duty payable on final product.
- (c) Cenvat is available instantly on receipt of inputs/ payment of input service and Cenvat credit may be utilised even before inputs/input services on which Cenvat is availed are actually used in production.
- (d) Rule 4(4) of Cenvat Credit Rules provides that depreciation should not be claimed on Cenvat credit availed.
- (e) Credit on inputs and capital goods can be taken as soon as goods are received in the factory.
- (f) In case of service tax, credit can be availed only after payment of Bill is made to the person who had provided input service.
- (g) Credit of education Cess and NCCD can be utilised for payment of education Cess and NCCD only.
- (h) Valuation of stock of inputs, WIP and finished goods also needs consideration.

Conflict between AS-2 and section 145A - As per section 145A of Income Tax Act, stock valuation should be inclusive of any tax, duty, cess or fee actually paid by assessee to bring the goods to the place of its location and condition as on date of valuation, even if such tax or duty is refundable. Thus, duty paid on inputs will have to be added while valuing stock, even if Cenvat credit is availed of such duty paid. In respect of finished stock, excise duty payable should be added to the inventory valuation even if not paid as goods are still lying in the factory. Both opening as well as closing stock should be valued on same basis.

However, as per Accounting Standard of ICAI (AS-2), inventory cost should comprise of all cost of purchases, cost of conversion and other costs incurred in bringing the inventories to the

present location and condition. Cost of purchase consists of purchase price including duties and taxes (other than those subsequently recoverable by the enterprise from the taxing authorities), freight inwards and other expenditure directly attributable to such acquisition. Trade discounts, rebates, duty drawbacks and other similar items are deducted in determining the costs of purchase. Cost of purchases should be exclusive of duties which are recoverable from the taxing authorities. (e.g. Cenvat). Inventory should be valued at lower of cost or net realisable value. Inventory should be valued on FIFO (First in First Out) method or weighted average method. [LIFO is not permitted].

If Cenvat credit of duty paid on inputs is not available for any reason, the closing stock should be valued inclusive of duty paid on inputs. [Guidance Note of ICAI on Accounting Treatment of Modvat / Cenvat - September 2000 issue of Chartered Accountant].

Thus, for purposes of Income Tax, inventory is required to be valued inclusive of excise duty, even if assessee is entitled to get Cenvat credit of duty. However, for purposes of balance sheet as per Companies Act, inventory should be valued exclusive of excise duty, if assessee is entitled to get Cenvat credit of duty paid on inputs.