

MOCK TEST PAPER – 2
FINAL COURSE: GROUP – II
PAPER – 8: INDIRECT TAX LAWS
SUGGESTED ANSWERS / HINTS

1. (a) Computation of CENVAT credit available to MNO Co. Ltd. for purchases made during the month of March, 2012:

Particulars	CENVAT credit available (₹)
Raw materials	52,000
Manufacturing machine (1,00,000 × 50%) (Note – 1)	50,000
Greases	10,000
Paint	<u>5,000</u>
CENVAT credit available	<u>1,17,000</u>

Notes:

1. As per third proviso to rule 4(2)(a) of the CENVAT Credit Rules, 2004, assessee eligible for SSI exemption can avail CENVAT credit of the whole amount of the duty paid on the capital goods in the same financial year in which such goods are received. However, since MNO Co. Ltd. is not eligible for SSI exemption, CENVAT credit of only 50% is available in respect of the manufacturing machine in the year of purchase.
 2. High Speed Diesel Oil is not an input as per the definition of inputs under rule 2(k) of the CENVAT Credit Rules, 2004. Hence, it is not eligible for the CENVAT credit.
 3. Office equipment is not a capital good as per the definition of capital goods under rule 2(a) of the CENVAT Credit Rules, 2004.
 4. It is assumed that the excise duty paid on various items includes education cess and secondary and higher education cess.
- (b) As per rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, the value of the excisable goods used for captive consumption is 110% of the cost of production of such goods. The cost of production has to be computed as per the Cost Accounting Standard (CAS)-4.

Computation of cost of production as per CAS-4 and value of the excisable goods:-

Particulars		₹
Cost of direct materials	₹ 16,545	
Less: Central excise duty	₹ <u>1,545</u>	15,000
Cost of direct employees		12,300
Work overheads		8,400
Quality control cost		4,300
Research and development cost		2,700
Administrative cost (production related)		<u>3,000</u>
Total		45,700
Less: Scrap value realized		<u>1,500</u>
Cost of production as per CAS-4		<u>44,200</u>
Value of excisable goods [44,200× 110%]		48,620

Notes:

1. It has been assumed that CENVAT credit is available on central excise duty paid on direct materials and hence, it has been deducted from the cost of direct materials in accordance with Cost Accounting Standard-4.
 2. Administrative overheads in relation to activities other than manufacturing activities have not been included in cost of production [CAS-4].
 3. Selling and distribution cost have been excluded from the cost of production as they are not in relation to production activity [CAS-4].
- (c) (i) Service tax is required to be paid only on the value/amount of taxable service received and not on the gross amount billed to the client. However, where the amount received is less than the gross amount charged/billed to the client, the assessee is required to amend the bills either by rectifying the existing bill or by issuing a revised bill and by properly endorsing such change in the billed amount.

Assuming that Mr. Mandeep has amended the bill, amount of service tax payable shall be computed by back calculations. Effective rate of service tax is 12.36% (12% service tax + 2% Primary Education Cess & 1% Secondary & Higher Education Cess on service tax).

Service tax and education cess payable	= $\frac{\text{Gross value} \times \text{Rate of tax}}{100 + \text{rate of tax}}$
	= $\frac{26,000 \times 12.36}{100 + 12.36} = ₹ 2,860/-$

- (ii) Section 68 casts the liability to pay service tax upon the service provider or upon the person liable to pay service tax as per Rule 2(1)(d). This liability is not contingent upon the service provider realizing or charging the service tax at the prevailing rate. The statutory liability does not get extinguished if the service provider fails to realize or charge the service tax from the service receiver.

However, sometimes it may happen that the assessee is not able to charge service tax because of the nature of service or he fails to recover the service tax from the client/customer as he is not aware that his services are taxable. Hence, in these cases the amount recovered from the client in lieu of having rendered the service will be taken to be inclusive of service tax and accordingly tax payable will be calculated by making back calculations.

Value of taxable service = $[\text{Gross amount charged} / (100 + \text{rate of tax})] \times 100$

Service tax = $[\text{Gross amount charged} / (100 + \text{rate of tax})] \times \text{rate of tax}$. Effective rate of service tax is 12.36%.

Service tax and education cess payable	$= \frac{\text{Gross value} \times \text{Rate of tax}}{100 + \text{rate of tax}}$
	$= 25000 \times 12.36 / 112.36$
	$= ₹ 2,750$

- (d) **Computation of the tax liability for the period March 1, 2012 to March 31, 2012:-**

	₹
Inputs purchased in the month [12.5% VAT]	1,00,000
Output sold in the month (within the State)	2,00,000
Inter-State sales	1,00,000
Input credit (including capital goods) (₹ 12,500 + ₹ 12,500)	25,000
Output tax	8,000
CST for Inter-State sale @ 2%	2,000
State VAT liability (₹ 8,000 – ₹ 25,000)	Nil
Excess credit carried forward to subsequent month	17,000
Central sales tax to be paid (₹ 2,000 – ₹ 17,000)	Nil
Excess credit carried forward to subsequent period	15,000

(e) Computation of assessable value of machine for customs duty:-

FOB price of the machine	US\$ 10,000.00
Add: Air freight (Maximum 20% of FOB) (Note-1)	US\$ 2,000.00
Insurance charges (1.125% of FOB) (Note-2)	US\$ <u>112.50</u>
Value (excluding local agent commission)	<u>12,112.50</u>
CIF value in Indian rupees = (Rs.12,112.5 × 45)	₹ 5,45,062.5
Add: Local agent commission (Note-4)	<u>10,000</u>
CIF Value	5,55,062.5
Add: Landing charges (1% of CIF) (Note-6)	<u>5,550.62</u>
Assessable value	<u>5,60,613.12</u>
Assessable value (rounded off)	<u>₹5,60,613</u>

Notes:

1. Air freight cannot exceed 20% of FOB value of the goods [Second proviso to rule 10(2) of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007]
 2. Cost of insurance is taken at 1.125% of FOB value of the goods [First proviso to rule 10(2)].
 3. Cost of local transport is not includible in assessable value as it is a post importation activity.
 4. Local agent commission is not a buying commission and hence, includible in assessable value [Rule 10(1)(a)].
 5. Cost of development work in India is not includible in the assessable value [Rule 10(1)(b)].
 6. Landing charges should be 1% of CIF value [First proviso to rule 10(2)].
2. (a) (i) The said statement is not valid. Rule 6 of CENVAT Credit Rules, 2004 has been amended vide **Notification No. 18/2012-CE (NT) all dated 17.03.2012** which provides that the rate of reversal for exempted goods has been revised from 5% to 6% .
- (ii) The said statement is absolutely valid. Rule 4 of the CENVAT Credit Rules, 2004 has been amended vide **Notification No. 18/2012-CE (NT) all dated 17.03.2012** to provide that CENVAT credit in respect of capital goods may be taken by the provider of output service when the capital goods are delivered to such provider, subject to maintenance of documentary evidence of delivery and location of the capital goods.

(b) The following procedure is to be followed by Mr. X for electronic refund through ICES system.

(i) Mr. X should

(a) have a bank account and also a central excise registration or service tax code number* and the same should be registered with Customs ICES, and

(b) declare his option to avail service tax refund on the electronic shipping bill/bill of export while presenting the same to the proper officer of Customs.

***Note:** Service tax code number shall be obtained by filing a declaration in Form A-2 to the jurisdictional Assistant Commissioner / Deputy Commissioner of Central Excise.

(ii) Service tax paid on the services eligible as refund under this exemption should be calculated electronically by the ICES system, by applying the rate specified in the schedule against the said goods, as a percentage of the FOB value.

(iii) Refund should be deposited in the bank account of Mr X.

(iv) Further, Mr. X who has claimed the refund electronically cannot claim the refund again on the basis of documents.

(v) Minimum service tax refund for an electronic shipping bill is ` 50.

(c) As per Baggage Rules 1998, a passenger is entitled to bring certain goods in India on duty free basis.

The basic allowance to Mr. Mayank consists of:

(i) Used personal effects, excluding jewellery required for satisfying daily necessities of life.

(ii) Other articles which are carried on the person or in his accompanying baggage.

There is no value limit for used personal daily necessities of life. However, there is a value limit in respect of other articles of baggage as categorized according to age of the passenger, country from which they returning and the number of days of stay abroad. For the passengers coming from Countries other than Nepal, Bhutan, Myanmar or China, where the age of passenger is upto 10 years and duration of stay is more than 3 days, the articles upto the value limit of Rs. 15,000 are allowed to be cleared duty-free.

In the light of aforesaid discussion, apparels and other articles brought by Mr. Mayank are allowed to be cleared duty- free.

3. (a) No, the show cause notice is not sustainable in law. The facts of the case are similar to the case of *Larsen & Toubro Ltd. v. UOI* 2009 (243) E.L.T. 662 (Bom.). The High Court opined that mere bringing of the duty paid parts in an unassembled form at one place, i.e. at the site, does not amount to manufacture of a plant. Simply collecting together at site the various parts would not amount to manufacture unless an excisable movable product (say a plant) comes into existence by assembly of such parts.

In the present case, as the petitioner had stated that the waste water treatment plant did not come into existence unless all the parts were put together and embedded in the civil work. Waste water treatment plant did not become a plant until the process which included the civil work, was completed. Thus, the Court held that no commercial movable property came into existence until the assembling was completed by embedding different parts in the civil works. Accordingly, since waste water treatment plant was not a separate movable marketable good and came into existence only on assembly of parts in the civil work, there was no question of levying excise duty on it.

- (b) Section 67 states that value of any taxable service is the gross amount charged by the service provider for the taxable services rendered by him. The labour contractor charges to the principal employer for the wages of his labour plus his service charges for arranging the labour.

Further, the department has clarified vide *M.F. (D.R.) Letter F.No.B1/6/2005-TRU dated 27.07.2005* that service tax is to be charged on the full amount of consideration for the supply of manpower, whether full-time or part-time. The value includes recovery of staff costs from the recipient e.g. salary and other contributions. Even if the arrangement does not involve the recipient paying these staff costs to the supplier (because the salary is paid directly to the individual or the contributions are paid to the respective authority) these amounts are still part of the consideration and hence form part of the gross amount.

Hence the taxable amount is the entire amount i.e. ₹ 1,85,000.

- (c) The action proposed by the Department is correct in law. The facts of the case are similar to *CCus. v. Hewlett Packard India Sales (P) Ltd. (2007) 215 ELT 484 (SC)*.

In this case, the Supreme Court observed that the pre-loaded operating system recorded in HDD in the laptop (item of import) forms an integral part of the laptop as the laptop cannot work without the operating system. A laptop without an operating system is like an empty building. Hence, laptop should be treated as one single unit and assessed accordingly.

However, if the operating system had been imported as packaged software like an accessory, then the benefit of exemption notification would have been available on it.

4. (a) The question whether for the purpose of computing interest on delayed refunds under section 11BB, the period commences with the date of receipt of application for refund or date on which the order of refund is made was examined by the Apex Court in the case of ***Ranbaxy Laboratories Ltd. v. UOI 2011 (273) E.L.T. 3 (SC)***. The Apex Court observed that interest under section 11BB becomes payable, if on an expiry of a period of three months from the date of receipt of the application for refund, the amount claimed is still not refunded.

The Apex Court further noted that Explanation appearing below the proviso to section 11BB introduces a deeming fiction that where the order for refund of duty is not made by the Assistant Commissioner/Deputy Commissioner of Central Excise but by an Appellate Authority or the Court, then for the purpose of this section the order made by such higher Appellate Authority or by the Court shall be deemed to be an order made under section 11B(2). It is apparent that the explanation does not have any bearing or connection with the date from which interest under section 11BB becomes payable and does not postpone the said date.

In the light of the aforesaid discussion, the Supreme Court elucidated that section 11BB of the Central Excise Act, 1944 comes into play only after an order for refund has been made under section 11B. However, the liability of the revenue to pay interest under section 11BB commences from the date of expiry of three months from the date of receipt of application for refund under section 11B(1) and not on the expiry of the said period from the date on which order of refund is made.

- (b) Yes, the view taken by the Department is correct in law. The facts of the above case are similar to the case of ***CCE v. Idea Mobile Communications Ltd. 2010 (19) STR 18 (Ker.)***.

The High Court, while examining the functioning of a SIM Card, admitted that SIM card is a computer chip having its own SIM number on which telephone number can be activated. SIM card is a device through which customer gets connection from the mobile tower. Unless the SIM card is activated, service provider cannot give service connection to the customer because signals are transmitted and conveyed through towers and through SIM card communication signals reach the customer's mobile instrument. Hence, it can be inferred that it is an integral part required to provide mobile service to the customer.

Further, SIM card has no intrinsic value or purpose other than use in mobile phone for receiving mobile telephone service from the service provider. Thus, the Court accepted the view that SIM cards, were not goods sold or intended to be sold to the customer, but supplied as part of service. Consequently, it held that the value of

SIM card supplied by the assessee would form part of the value of taxable service on which service tax was payable by the assessee.

- (c) Yes, the contention of the assessee is justified in law. The facts of the given case are similar to the case of **Atherton Engineering Co. Pvt. Ltd. v. UOI 2010 (256) ELT 358 (Cal.)**. In the instant case, the Court noted that it was the use of the product that had to be considered in the instant case. If a product undergoes some change after importation till the time it is actually used, it is immaterial, provided it remains the same product and it is used for the purpose specified in the classification. Therefore, in the instant case, it examined whether the nature and character of the product remained the same.

The Court opined that if the embryo within the egg was incubated in controlled temperature and under hydration, a larva was born. The larva did not assume the character of any different product. Its nature and characteristics were same as the product or organism which was within the egg.

Hence, the Court held that the said product should be classified as feeding materials for prawns under the heading 2309. These embryos might not be proper prawn feed at the time of importation but could become so, after incubation.

5. (a) (i) Section 2(d) of the Central Excise Act, 1944 defines “excisable goods” as goods specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985 as being subject to a duty of excise and includes salt. An explanation to Section 2(d) of the Central Excise Act, 1944 states that the expression “goods”, for purpose of the said clause, includes any article, material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable.

Goods which are not listed in Tariff or goods which are mentioned in Tariff, but the column of rate of duty is blank are non-excisable goods, e.g. water (there is no entry in Tariff). Excise law is not applicable on non excisable goods.

“Non-dutiable goods” are excisable goods listed in Excise Tariff. Excise law is applicable to them, but they are not liable to excise duty. Non dutiable goods may be of two types-

- (a) Nil duty goods-Tariff rate for such goods is nil, and
- (b) Exempted goods-100% exemption is available under section 5A. for such goods.

- (ii) As per section 4(3)(c) of the Central Excise Act,1944, “place of removal” means –

- (a) a factory or any other place or premises where excisable goods are being produced or manufactured
- (b) a warehouse or any other place or premises wherein the excisable goods

have been permitted to be deposited without payment of duty

- (c) a depot, premises of a consignment agent or any other place or premises from where the excisable goods are to be sold after their clearance from the factory
- (b) (i) The provisions of rule 4 of the Service Tax (Determination of Value) Rules, 2006 are as under:-
 - (a) The Central Excise Officer is empowered to satisfy himself as to the accuracy of any information or document furnished for valuation. The provisions of rule 3 do not restrict or put to question such power of the Central Excise Officer.
 - (b) The Central Excise Officer can reject the value determined by the service provider and issue a show cause notice to him, if he is of the opinion that the value determined by such service provider is not in accordance with the provisions of the Finance Act, 1994 or these rules. The service provider would then be required to show cause why the value of taxable service should not be fixed at the amount specified in such notice.
 - (c) The Central Excise Officer, after giving such service provider an opportunity of being heard, will determine the value of such taxable service in accordance with the provisions of the Finance Act, 1994 and these rules.
- (b) (ii) VAT invoice is a document providing details of goods sold along with price, tax charged and other details as may be prescribed. Vat invoice is issued by a dealer authorized under the Act. Mandatory provisions to be complied with:
 - (a) Every registered dealer whose turnover of sales exceeds the specified amount shall issue to the purchaser a serially numbered tax invoice, cash memo or bill with the prescribed particulars.
 - (b) The VAT invoice shall be dated and signed by the dealer or his regular employee, showing the required particulars.
 - (c) The dealer shall keep a counterfoil or duplicate of such VAT invoice duly signed and dated.

(c) Significance of Indian Customs Waters

- (i) If an officer of customs has reason to believe that any person in India or within the Indian customs waters has committed an offence punishable under section 132 or section 133 or section 135 or section 135A or section 136, he may arrest such person informing him of the grounds for such arrest. [Section 104 of Customs Act]
- (ii) Where the proper officer has reasons to believe that any vessel in India or

within Indian customs waters has been used in the smuggling of any goods or in the carriage of any smuggled goods, he may stop any such vehicles, animal or vessel or in case of an aircraft, compel it to land. [Section 106 of Customs Act].

- (iii) Any vessel which is or has been within the Indian customs waters is constructed, adapted, altered or fitted in any manner for the purpose of concealing goods shall be liable to confiscation. [Section 115(1)(a) of Customs Act].
- (iv) Customs Officer has the power to search any person who has landed from/about to board/is on board any vessel within Indian customs waters and who has secreted about his person, any goods liable to confiscation or any documents relating thereto. [Section 100(2)(a) of Customs Act].
- (v) Any goods which are brought within the Indian Customs Waters for the purpose of being imported from a place outside India, contrary to any prohibition imposed by or under this Act or any other law for the time being in force, shall be liable to confiscation. [Section 111(d) of Customs Act].

Note: Any three points may be mentioned.

- 6. (a)** The procedure for warehousing of goods removed from a factory is detailed below:
- (i) The consignor shall prepare an application for removal of goods from a factory to a warehouse in quadruplicate and also prepare an invoice for goods to be warehoused.
 - (ii) He has to send original, duplicate and triplicate application and duplicate invoice along with goods to the warehouse of destination. The quadruplicate copy of application has to be sent to the Superintendent of Central Excise in-charge of his factory within 24 hours.
 - (iii) Within 24 hours of receipt of the goods the consignee shall verify the goods with all the copies of application.
 - (iv) The consignee has to send:
 - (a) Original copy to Superintendent-in-charge of his warehouse.
 - (b) Duplicate copy of consignor and retain the triplicate for record.
 - (v) The Superintendent-in-charge of the warehouse shall countersign the application received by him and send the same to Superintendent-in-charge of the consignor.
 - (vi) The consignor shall retain the duplicate application duly endorsed by the consignee for his record.

OR

- 6. (a) (i)** Annual Financial Information Statement is a return to be submitted in Form-ER-4. It is to be submitted by every assessee to the Superintendent of Central Excise for the preceding financial year by 30th November of the succeeding year [Rule 12(2)(a) of the Central Excise Rules, 2002].

The following assessees have been exempted from such submission of ER-4 :

- (a) An assessee who pays less than Rs.1 crore of excise duty during the financial year to which ER-4 relates.
 - (b) Indian Ordinance Factories, Department of Defence Production and Ministry of Defence.
- (ii)** If the assessee does not agree to the classification or assessable value of goods determined by the excise authorities, he can file an appeal and till the time the appeal is decided, can pay the duty under protest if no stay is obtained from Appellate Authorities. However, if the appeal is not decided in his favour and the appellate remedy is exhausted, the assessee will lose the right to pay duty under protest. The time limit of one year for claiming refund of excise duty does not apply if duty is paid under protest.

The assessee will inform the Superintendent/Inspector of Central Excise that he is paying duty under protest in writing. He will mark invoices or monthly/quarterly returns indicating the goods on which duty is paid as 'under protest'. In case of lump-sum duty payment of past demand, he may record the fact of duty payment under protest in the PLA, CENVAT account or Daily Stock Account.

- (b) (i)** As per section 96C of Finance Act, 1994 an advance ruling can be sought in the following matters:
- (a) classification of any service as a taxable service under Chapter V of Finance Act, 1994;
 - (b) the valuation of taxable services for charging service tax;
 - (c) the principles to be adopted for the purposes of determination of value of the taxable service under the provisions of Chapter V;
 - (d) applicability of notifications issued under Chapter V;
 - (e) admissibility of credit of service tax.
 - (f) determination of the liability to pay service tax on a taxable service under the provisions of Chapter V.
- (ii)** VAT registration can be cancelled in following circumstances:
- (a) discontinuance of business; or

- (b) disposal of business; or
 - (c) transfer of business to a new location; or
 - (d) annual turnover of a manufacturer or a trader dealing in designated goods falls below the specified amount.
- (c) Section 72 of the Customs Act provides that in any of the following circumstances the goods shall be considered to have been removed improperly from a warehouse –
- (i) where any warehoused goods are removed from a warehouse in contravention of section 71 of the Customs Act;
 - (ii) where any warehoused goods have not been removed from a warehouse at the expiration of the period during which such goods are permitted under section 61 to remain in a warehouse;
 - (iii) where any warehoused good have been taken under section 64 as samples without payment of duty;
 - (iv) where any goods in respect of which a bond has been executed under section 59 and which have not been cleared for home consumption or exportation are not duly accounted for to the satisfaction of the proper officer.
7. (a) (i) As per rule 2(a)(i) of the Interpretative Rules to First Schedule of the Central Excise Tariff, if any particular heading refers to a finished/complete article, the incomplete/unfinished form of that article would also be classified under the same heading provided the incomplete/unfinished goods have the essential characteristics of the finished goods.
- (ii) The officer-in-charge of the warehouse may permit waiver from physical warehousing (i.e. permitting export without physically storing the goods in the warehouse) where the exporter so requests in writing. However, aforementioned permission will be given only if the formalities relating to record-keeping are completed in usual manner with suitable record in the Warehouse Register: 'Warehousing waived'. It is to be kept in mind that aforesaid permission is given in the following exceptional cases:
- (a) where delay occurred due to delayed supply from the factory; or
 - (b) Longer transit period; or
 - (c) Requirement of immediate export; or
 - (d) Any other genuine reasons
- Besides, it is also essential that the entire consignment is entered for export in the original packing. Such cases of permission granted are required to be reported to the Superintendent-in-charge of the warehouse at the earliest.

- (b) (i) **Time limit for issuing an invoice/bill/challan:** As per Rule 4A(1) of Service Tax Rules, 1994, an invoice is to be issued within 30 days from the date of completion of the taxable service or receipt of payment towards the value of taxable service, whichever is earlier.

Essential Particulars to be specified in an invoice/bill/challan: Further, in general following are the essential particulars to be specified on an invoice/bill/challan as per Rule 4A of Service Tax Rules, 1994:

- (a) The name, address and the registration number of the Service Provider;
- (b) The name and address of the Service Recipient;
- (c) Description, classification and value of taxable service provided or to be provided;
- (d) The service tax payable thereon.

- (ii) The following records should be maintained under VAT system:

- (a) Purchase records
- (b) Sales records
- (c) VAT account containing the details of output tax and input tax together with credit and debit notes issued during the period
- (d) Separate record for exempt sale

The following records should also be kept and produced to an officer:-

Copies of invoices, debit and credit notes issued, all purchase invoices, details of tax charged on purchases and sales, total output tax, input tax and net tax for each period, details of goods manufactured and delivered from the factory, details of each supply of goods from the business premises. Failure to keep these records may attract penal provisions under the State VAT law.

- (c) Section 17 of the Customs Act, 1962 stipulates that after bill of entry or shipping bill has been presented, the proper officer may examine and test the goods. After such examination and testing, the proper officer assesses the duty leviable on such goods.

Under the first appraisal system, the goods are examined first and then they are assessed. The appraiser normally resorts to this method if he is not able to make assessment on the basis of declaration made in the bill of entry or shipping bill and the documents submitted along with them and deems that inspection is necessary. The importer himself may also request first check procedure, if he cannot give all required details regarding description/value of goods. He has to make request for first check examination at the time of filing of bill of entry.

Under the second appraisement system, the information and documents furnished by the importer are adequate to determine the correct tariff nomenclature, tariff classification and valuation of the goods for purposes of assessment. In such a situation, physical examination of the goods or their weighment or testing is only a confirmatory check. Under this system, such an examination is carried out after assessment and collection of duty.