

NOTES ON APPLICATION OF COST ACCOUNTING STANDARDS-4

(See Rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000)

COMPILATION

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- ☐ Member, finance Committee DMA
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- ☐ Member EC, ASSOCHAM
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CHAPTER – 1

Valuation under Central Excise

The scheme of valuation of excisable goods is dealt under Sec. 3A, Sec. 4 and Sec. 4A of the Central Excise Act, 1944. The goods manufactured have to be valued in a prescribed manner as per said provisions to determine the liability to pay excise duty by the assessee. Section 3 provides that excise duties shall be levied and collected on all excisable goods which are produced or manufactured in India at the rates set forth in Schedule to the Central Excise Tariff Act, 1985. Section 4 provides the mechanism to determine the value of goods subject to duty for the purpose of assessment. Section 4A provides for valuation of excisable goods with reference to retail sale price and applicable to commodities as notified by the Government from time to time and on which retail price is required to be indicated under the provision of the Standard of Weights & Measures Act, 1976 and the Rules made there under.

Section 4(1) (a) of Central Excise Act, 1944 deals with the Valuation of excisable goods when following requirements are satisfied:

1. Goods are sold at the time and place of removal from factory/warehouse;
2. The assessee and the buyer of the goods are not related; and
3. The price is the sole consideration of sale.

Each transaction is treated as a separate transaction for valuation purposes.

If any one of the above requirements is not satisfied, assessable value shall be determined under the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 notified on 30.6.2000, as provided under Section 4(1)(b) of the Act.

Meaning of Captive Consumption

The word '**Captive Consumption**' refers to goods produced or manufactured in a factory and used within the factory in the manufacture of other goods. When goods manufactured by one division/plant are transferred to and consumed by another division/plant of the same organization or related undertaking for manufacturing another product(s), such goods are also said to be captively consumed.

In many cases during the manufacture, certain intermediate goods also emerge. These intermediate goods are further used in manufacture of other goods and are covered in the meaning of '**Captive Consumption**'. Sometimes the goods are not removed from the factory but are used in the further manufacture of goods in such cases duty is payable as soon as the goods are manufactured within the factory, if not exempted. However, the goods captively used in the same factory of the manufacturer are exempted from duty as per Notification No. **67/ 95-CE dt. 16.03.1995** viz., the manufacturer of Motor Vehicles may also manufacture various parts of the Motor Vehicles like brakes, panels etc. These parts are also excisable goods and have separate entry in the schedule to Central Excise Tariff Act, 1985. If

these parts are removed from the factory, duty is payable but if these parts are further used in the same factory of the manufacturer in the assembly/further manufacture of Motor Vehicles, then the use of parts and components is called as captive consumption.

Similarly, during the manufacturing process, certain by-products, waste and scrap also get generated. These may be either sold or recycled or transferred for captive consumption in other products. By-products, waste and scrap are incidentally automatically generated during the manufacturing process. Generation of by-products, waste and scrap is incidental to the achievement of the basic objective of producing satisfactory / acceptable products. It arises as an inevitable consequence of operation. As per normally accepted cost accounting principle, the total cost of production i.e. raw material cost and conversion cost is charged to good saleable products. Therefore, no part of the cost remains to be absorbed/ charged to by-product, scrap/waste.

Keeping this in view, **Cost Accounting Standards -4 (CAS 4)**, issued by the Institute of Cost Accountants of India, has also provided for reducing the realizable value of by-product, scrap/waste etc. from the cost while computing cost of production for captive consumption in the product cost sheet.

CHAPTER – 2

Valuation in the case of Goods where whole or part of the excisable goods are not sold but Captively Consumed

The provisions regarding valuation of goods where whole or part of the excisable goods are not sold but captively consumed are given in **Rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000**. Prior to **Notification No, 14/2013- Central Excise (N.T.) dated 22nd November, 2013**, valuation under rule 8 mainly referred to goods where no part sale was effected or such goods which were wholly consumed within the unit. The Rule now provides that where whole or part of the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value of such goods that are consumed shall be **one hundred and ten per cent** of the cost of production or manufacture of such goods.

On the introduction of **Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, w.e.f. 1st of July 2000**, the general principles of costing were referred as the basis for the valuation. This clarity was made by the Board vide **Circular No.354/81/2000-TRU dated 30 June 2000**, that in order to value goods which are captively consumed, the general principles of costing would be adopted for the application of Rule 8.

The Central Board of Excise and Customs interacted with the Institute of Cost Accountants of India to develop costing standards for the costing of the cost of goods used for captive consumption. The Institute of Cost Accountants of India (ICAI-CMA), since then has developed nineteen cost accounting standards out of which three namely, CAS-2 on Capacity Determination, CAS-3 on Overheads and CAS-4 on Cost of Production for Captive Consumption, were released on 13rd February, 2003 by CBEC jointly with ICAI-CMA.

By **Circular No. 692/8/2003-CX, dt.13.2.2003** the Board clarified that cost of production of captively consumed goods will henceforth be done strictly in accordance with (Cost Accounting Standard-4). This standard has been formulated by the Institute of Cost Accountants of India and prescribes elaborate components of cost and adding of overheads also. It may therefore be appropriate for the assessee to obtain a certificate by a Cost Accountant in practice indicating the cost of production of the captively consumed goods.

Periodicity of the Certificate

It is nowhere provided that when or at what interval a certificate by a cost accountant be obtained. The Circular No. 643/34/2002-CX dated 1st July, 2002 provides clarification for removal of doubts. The Sl.No.5 of the clarificatory circular provides that:-

“ If the same goods are partially sold by the assessee and partially consumed captively, the goods sold would be assessed on the basis of “ transaction value” [provided they meet the condition of sec.4(1)(a)] and the goods captively consumed would be valued as per Rule 8 of the valuation rules. This is because as per new Section 4 transaction value has to be determined for **each removal**.”

The Institute of Cost Accountants of India in its Guidance note on CAS-4, opines that:-

“The basic purpose of CAS-4 is to determine the cost of production for goods capitively consumed and calculate deemed transaction value thereof. Therefore, valuation is required at the time of removal of the goods. If costing is for the future period, it will be done at projected costs and projected capacity utilisation. In such cases, valuation of opening and closing stock of WIP and finished stock is to be ignored. In case, when the normal capacity utilization is not quantifiable and / or actual capacity utilization is likely to be low, as compared to previous period; it may be advisable that the manufacturer shall go for Provisional Assessment under rule 7 of Central Excise Rules, 2002. After the end of the year annual certification should be done based on the finalized books of account and if the cost of production is found different than the provisional costs, differential duty shall be paid by the manufacturer”

Apparently CAS-4 certificate by a Cost Accountant confirming the duty liability and payment has to base upon final books of accounts. On the other hand transaction value has to be derived for each transaction. It is therefore practically not possible to fulfil both these requirements. The Institute of Cost Accountants of India has tried to address this issue to a limited extent by opining to follow the principles on provisional basis till the records are finalised and at the end of the year certification should be done based upon the finalized books of accounts and differential duty if any should be paid.

Keeping in view the requirements under section 4 of the Central Excise and CAS-4, one may obtain a a certificate either whenever there is material change in the input cost or as audit requirement. Since in most of the units / companies quarterly accounts are available, it is advisable to obtain a CAS-4 certificate for each quarter. This will further facilitate in the year end certificate or as a reference point for CAS-4 Certificate at any subsequent date.

Application of CAS-4:

The relevance of CAS-4 are in the following cases :

1. Where a manufacturer is manufacturing a product which is otherwise exempt from duty but in process of manufacture an intermediate product mentioned in the tariff, comes into existence which is dutiable. The intermediate goods which come into existence must discharge applicable duty before it gets cleared for factory / unit for the manufacture of the duty exempted final product. The value of duty in all such cases shall be on 'Cost + 10%' w.e.f 5 August, 2003. However, in cases where final product is dutiable then exemption **Notification No. 67/95, dt. 16.3.1995** shall apply.
2. Where whole or part of the excisable goods are not sold but captively consumed (amendment inserted vide **Notification No. 14/2013- Central Excise (N.T.) dated 22nd November,2013**.
3. In the case of samples etc. which are distributed free, as part of the marketing strategy, or as gifts or as donations: Since the goods are not sold, Section 4(1)(a) will not apply and recourse will

have to be taken to the Valuation Rules. No specific rule covers such a contingency. Except Rule 8 all other rules cover contingencies where sale is involved in some form or the other. Therefore the residuary Rule 11 will have to be adopted along with the spirit of Rule 8. In other words, the assessable value would be 110% of the cost of production or manufacture of the goods.

4. Where Rule 9 and 10 of the **Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000** dealing with determination of assessable value in case of sale to related person apply.

In a landmark judgment in the CASE NO.: Appeal (civil) 2947-2948 of 2001 (**Commissioner of Central Excise, Pune v/s M/s. Cadbury India Ltd**, delivered on 01/08/2006 the Hon'ble Supreme Court of India, observed that 'the Institute of Cost and Works Accountants of India (ICWAI) has laid down the principles of determining cost of production for captive consumption and formulated the standards for costing : CAS-4.

According to CAS-4 the **definition of "cost of production"** is as under :

"Cost of Production: Cost of production shall consist of Material Consumed, Direct Wages and Salaries, Direct Expenses, Works Overheads, Quality Control cost, Research and Development Cost, Packing cost, Administrative Overheads relating to production."

The cost accounting principles laid down by ICWAI have been recognized by the Central Board of Excise and Customs vide Circular No.692/8/2003 CX dated 13.2.2003. The circular requires the department to determine the cost of production of captively consumed goods strictly in accordance with CAS-4.

The Tribunal in the case of **BMF BELTINGS LTD. vs. CCE : 2005 (184) E.L.T. 158 (Tri. Bang.)** for the period 1995 to 2000 has directed the department to apply CAS-4 for the determination of the cost of production of the captively consumed goods. In **ITC vs. CCE (190) ELT 119** the Tribunal held that the department has to calculate the cost of production in terms of CAS-4. Other decisions of the Tribunal, wherein it has directed that CAS-4 be applied for determination of the cost of production, are **Teja Engineering v/s CCE 2006 (193) ELT 100 (Tri-Chennai)**, **Ashima Denims v/s CCE 2005 (191) ELT 318 (Tri-Mumbai)**, and **Arti Industries vs. CCE 2005 (186) ELT 208 (Tri-Chennai)**. It is therefore a consistent view taken by the Tribunal. The department has not filed any appeal in these cases and accepted the legal position. Apart from this, in the light of several decisions of this Court, the Department is also bound by the said Circular No.692/8/2003 CX dated 13.2.2003 issued by the CBEC. As such it cannot now take a contrary stand.

The observations made by the Supreme Court is consistent with the views expressed by the Tribunals that though CAS-4 was issued on 13.2.2003, cases pending finalization for the period earlier to this, may be considered in line with costing principles laid down in CAS-4, issued by the Institute of Cost and Works Accountants of India. Assessments finalized prior to 13 February, 2003, not to be opened:

A clarification was issued by the Chief Commissioner, Chennai, Zone **stating that cases which have been finalized prior to 13.2.2003 should not be opened for application of CAS-4**. The extracts of the letter is being reproduced below:

‘Copy of letter **C.No. IV/16/92/2003-Cx.Pol dated 05.09.2003** of this office.

Please refer to the Board’s circular No. 692/8/2003-CX-I (F.No. 6/29/2002- CX-I) dated 13.02.2003 communicating acceptance of cost Accounting Standard-4 (CAS-4) for the purpose of valuation of the excisable goods which are captively consumed under Rule 8 of Central Excise Valuation (Determination of price of Excisable goods) Rules, 2000.

The field formations have raised certain doubts as to whether the above said CAS-4 could be applied to all pending assessments. It is observed from the above cited circular of the Board that the principles of CAS costing are to be adopted w.e.f, 13.2.2003 and therefore the assessments pending finalization on 13.02.2003 will also be covered under CAS-4. Assessments already finalized prior to 13.02.2003 on the basis of Board’s Circular 258/92/96 CX dated 30.10.96 are not required to be reopened. The field officers in this Commissionerates have been advised accordingly. Kindly confirm.’

Therefore it shall be fair to say that in view of the above circular and decision of the Hon’ble Supreme Court of India, application of Cost Accounting Standard-4 or CAS-4, is on all cases whether before or after 13 thFebruary,2003 except where cases have been finalized prior to 13.2.2003.

CHAPTER - 3

Valuation of Goods if Sale to Related Person

The **Rule 9** of the **Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000** specifies that the goods can be sold to related persons for two purposes, one for onward sale when the related person is dealer distributor of the assessee and secondly the related person buys goods from the assessee for consumption in the production or manufacture of articles. Whenever the related person does not sell the goods but uses or consumes such goods in the production or manufacture of the articles, the value shall be determined in the manner specified in rule 8.

Rules 8, 9 and 10 of the **Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000** dealing with determination of assessable value in case of captive consumption and sale to related person have been amended vide notification no. 14/2013 – Central Excise (N.T.) dated 22.11.2013 to clearly state that these rules apply irrespective of whether the whole or a part of the clearances of manufactured goods are covered by the circumstances given in these rules. Each clearance is required to be assessed according to section 4(1)(a) or the relevant rule dealing with the circumstances of clearance of the goods, as the case may be.

For example, if an assessee clears his goods in such a way that first removal of goods is to an independent buyers, some goods are captively consumed, second removal is to such a related person who is covered under rule 9 and third removal is to a person who is covered under rule 10, then the first removal should be assessed under section 4(1)(a), captively consumed goods should be assessed under rule 8, second removal should be assessed under rule 9 and third removal should be assessed under rule 10 of these rules. It may be noted that Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 are not required to be followed sequentially. Each of these rules provide for arriving at the assessable value of goods under different contingencies as noted by Hon'ble Supreme Court at paragraph 70 in case of **Commissioner of Central Excise, Mumbai vs M/s FIAT India Pvt Ltd** [2012 (283) ELT 161 or 2012-TIOL-58-SC-CX].

Serial No. 5, 12 and 14 of the Circular no. 643/34/2002-CX dated 1-7-2002 are nullified in view of the amendments in the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, as these amendments address the issues on which these clarifications were issued. **The amended rules and accordingly this circular shall apply with effect from 1st December, 2013.**

CHAPTER - 4

Cost Accounting Standards

In view of the need to bring in uniformity in the principles and methods used for determining the cost of production of excisable goods used for captive consumption, the Institute of Cost Accountants of India has prescribed the Cost Accounting Standard 4 (CAS-4). The said Standard provides the method of calculation of cost of production for captive consumption. This standard also aims at bringing in uniformity and transparency in the valuation of excisable goods.

The Central Board of Excise & Customs has recognized the importance of CAS-4 vide circular No. 692/08/2003-CX dt. 13.02.2003 (File No. 6/29/2002-CX.I), which states that calculation of cost of production of captively consumed goods will henceforth be done strictly in accordance with CAS-4 issued by the Institute of Cost and Works Accountants of India.

CHAPTER – 5

General Guidelines

In order to calculate the cost of production for captive consumption, it is necessary to understand that the method and accuracy of cost computation will be determined and impacted by the following factors:

1. The CAS 4 is applicable to the manufacturers who are registered under Central Excise, irrespective of the constitution of the organization. It does not make any difference whether the manufacturer falls in the category of proprietorship, partnership, co-operative sector, company etc.
2. Whether the product is covered under the Cost Accounting Records Rules issued in pursuant to Sec 209(1)(d) of the Companies Act, 1956? If the product is already covered under Cost Accounting Records Rules, the systems required for cost calculation would be in place and the relevant information will be readily available for such calculations. In case Sec 209(1) (d) of the Companies Act, 1956 is not applicable, it is suggested that the assessee may maintain the costing records as per the generally accepted costing principles.
3. The method of valuation of issues followed by the assessee be either lot-wise actual, FIFO or Weighted Average to determine the consumption rates of various input materials and the cost of materials consumed.
4. The level of compliance of Cost Accounting Standards: The principles stated in Cost Accounting Standards, are applicable for all Industries and the level of its compliance determines the adequacy of the costing system in the organization which in turn determines the accuracy of product cost calculation for captive consumption.
5. In case raw material is imported through advance license / DEPB or under any other scheme and used for manufacture of goods for captive consumption, adjustment for import duty has to be made to bring the raw material cost to the level of duty paid import. However, Duty Drawback refund/benefit shall not be reduced from the input cost. Other export benefits such as DEPB, DFRC, and DEEC will not be deducted for calculation of cost of production.
6. Periodicity of Certificates and basis for calculation of cost of production under CAS-4:

The basic purpose of CAS-4 is to calculate deemed transaction value of the goods captively consumed in the same unit or transferred to the other unit of the same manufacturer. The valuation (assessable value) is required at the time of removal of the goods. The circular no.975/09/2013-CX dated 25th November, 2013 has now further clarified that Section 4 of the Valuation of excisable goods for purposes of charging of duty of excise under the Act requires charging of duty with reference to value to each removal of goods.

Normally the costing will be for the future dispatches/period. It could be either for the existing product or in respect of a new product yet to be manufactured. In case of costing for the existing product, it will be worked out based on the actual cost for the previous quarter.

In case of costing for a new product, it will be calculated at projected cost, keeping in view projected normalized production and other cost parameters.

The frequency of revising the certificate of cost of production will depend upon the significance in the changes in the cost due to various factors like input cost fluctuations, changes in the employee cost and other expenses.

Valuation of opening stock and closing stock of WIP and Finished goods need not be considered in the above referred situations.

If the actual cost of production is to be worked out after the close of the year, then due consideration should be given to opening and closing stock of WIP and Finished goods.

7. In case of multi-locational units, the cost of production should be worked out separately for each unit taking into consideration material cost and overheads of the respective unit.

8. In case the assessee is manufacturing different varieties, sizes, etc. of goods, then cost of production for each of the variety/size should be worked out separately.

9. If duty is paid on intermediate products and final product is exempted, then at the year end actual costing should be worked out and differential duty to be recovered / refunded.

10. It is advisable for the assessee to obtain certificate from cost accountant before the removal of the goods.

11. Companies following standard costing system should adjust the variances to the various products as per normally accepted cost accounting principles for calculation of product wise actual cost.

CHAPTER – 6

Guidelines on various paras of Cost Accounting Standard-4

(Para numbers given below are as per CAS-4. Guidelines have been given under “**Notes**” in each para.)

2. Objective:

2.1 The purpose of this standard is to bring uniformity in the principles and methods used in determining the cost of production of excisable goods used for captive consumption.

2.2 The Cost Statement prepared based on standard will be used for determination of assessable value of excisable goods used for captive consumption.

2.3 The standard and its disclosure requirement will provide better transparency in the valuation of excisable goods used for captive consumption

3. Scope:

3.1 The standard is to be followed for determining the cost of production to arrive at an assessable value of excisable goods used for captive consumption.

Notes:

The situations in which CAS-4 can be used:

- Cost of production for captive consumption.
- Goods manufactured and transferred to project/sites for further work, e.g.. Erection, construction, etc.
- Job Work/Loan License production
- Principal to Principal manufacture in pharma and other industries-
- Free gifts for distribution as sales promotion, if sale price is not available.-
- Goods to be transferred to other units for further use in the manufacture of goods for export (even though excise duty is not payable). -
- Transfer/sale to related party/undertaking for captive consumption.

3.2 Cost of production will include various cost components. They are already defined in Cost Accounting Standard-1 (Classification of Costs- CAS-1). Thus, this standard has to be read in conjunction with CAS-1.

4. Definitions:

4.1 Cost of Production: Cost of production shall consist of Material Consumed, Direct Wages and Salaries, Direct Expenses, Works Overheads, Quality Control cost, Research and Development Cost, Packing cost, Administrative Overheads relating to production. To arrive at cost of production of goods dispatched for captive consumption, adjustment for Stock of work-in-Process, finished goods, recoveries for sales of scrap, wastage etc shall be made.

Note:

This definition deals with the elements of cost and income to be considered while calculating the cost of production for captively consumed goods.

4.2. Captive consumption: Captive Consumption means the consumption of goods manufactured by one division or unit and consumed by another division or unit of the same organization or related undertaking for manufacturing another product(s).

Note:

This definition specifies the scope for application of CAS-4 which has also been explained in para 3.1 above.

4.3 Normal capacity: Normal Capacity is the production achieved or achievable on an average over a period or season under normal circumstances taking into account the loss of capacity resulting from planned maintenance. (CAS-2)

Note:

This definition deals with the method of determining the normal capacity for absorption of fixed production overheads. (para 5.9)

CAS-2 defines Practical or achievable capacity as *“the maximum productive capacity of a plant reduced by the predictable and unavoidable factors of interruption pertaining to internal causes”*.

Thus, practical capacity is installed capacity minus the inevitable interruptions due to time lost for preventive maintenance, repairs, set ups, normal delays, weekly off days and holidays etc. Practical capacity does not consider external factors causing reduction in production e.g. lack of orders.

In other words, normal capacity is the installed capacity less all allowances for known unavoidable interruptions. In practice, practical capacity and normal capacity will be same.

5. Determination of cost of production for captive consumption

To determine the cost of production for captive consumption, calculation of different cost components and adjustments are explained below:

5.1 Material consumed: Material Consumed shall include materials directly identified for production of goods such as :

- (a) indigenous materials**
- (b) imported materials**
- (c) bought out items**
- (d) self manufactured items**
- (e) process materials and other items**

Cost of material consumed shall consist of cost of material, duties and taxes, freight inwards, insurance, and other expenditure directly attributable to procurement. Trade discount, rebates and other similar items will be deducted for determining the cost of materials. Cenvat credit, credit for countervailing customs duty, Sales Tax set off, VAT, duty draw back and other similar duties subsequently recovered/ recoverable by the enterprise shall also be deducted.

Notes:

Material cost consists of - Raw Material, process material, colours and chemicals and packing materials. Further, material can be also classified as direct material and indirect material. While direct material is a part of Material cost, indirect material can be allocated to the cost centres or to the product.

Raw material shall include – indigenous materials, imported materials, bought-out items and self-manufactured items.

With inventory accounting system in place, the material cost is already being arrived at, considering following two factors:

- (a) Quantity of material consumed; and**
- (b) Unit rate of material consumed**

Quantity of material consumed:

The quantity of material consumed is to be worked out from material issued from stores for such product. Such consumption in quantity may be derived by two methods. The selection of method will depend on the systems in vogue in the organization and the type of product manufactured.

Method (i): Based on actual issues for that batch, unit or job - This method is preferred as it establishes direct relationship of actual material usage for the product.

Method (ii): Based on any method other than actual e.g. Standard requirement - This method is to be used in case of goods, where the direct link of actual consumption for product is not available. The manufacturer using this method should certify the quantitative requirement considered for calculation of material consumption. Documents related to Bill of Material etc. may be verified by the cost accountant for this purpose. It may be ensured that usage variance is within reasonable limit and it should be adjusted in calculation of cost of production.

(b) Unit Rate of material consumed: The unit rate of material consumed is determined with respect to (i) the source / type of material consumed, and (ii) the method of valuation followed for issue of goods to production.

(i) Source/type of material consumed:

- (a) indigenous materials
- (b) imported materials
- (c) bought out items
- (d) self manufactured items
- (e) process materials, colours & chemicals, packing materials, etc.

It is advisable that the source of material consumed is linked to actual issues of material. In case of manufacturers, using the same item of direct material from different source either due to quality difference, supplier, capacity constraints or any other reason, it is essential to have this linking as the cost of the same item may be different, if procured from different sources.

(ii) Method of valuation followed for issue of goods to production:

It is advisable to work out cost of material consumed by lot wise cost or First In First Out (FIFO) or weighted average method of valuation of consumption as these methods are widely accepted. The actual consumption in value reported in the Profit and loss account is generally worked out by the following method:

Opening stock

Add - Purchases

Less - Closing stock

= Consumption

(a) Indigenous Material: The Landed Cost of indigenous material shall be calculated in the following manner.

Basic Material cost (after deducting discounts, if any)

Add: Excise Duty

Sales Tax/VAT

Turnover Tax

Surcharge etc.

Octroi /Entry Tax

Other levies

Other expenses directly attributable to procurement (Freight inwards, transit insurance, etc.)

Less: Cenvat Credit

Sales Tax/VAT Set Off

Other set offs directly attributable to the material.

(b) Imported Material: The landed cost of imported material shall be calculated in the following manner.

CIF value of Material

Add: Customs Duty

Surcharge

Additional Duty / Countervailing Duty

Special Additional Duty

Protective Duty

Anti Dumping Duty

Octroi / Entry Tax

Other levies

Other Exp. Directly attributable to procurement (Freight inwards, Local Freight, transit insurance, local insurance)

Other charges such as Customs clearance etc.

Less: Cenvat Credit (including CVD)

Other rebates, benefits recovered / recoverable etc.

DEPB, DEEC, DFRC

and other such export benefits shall not be reduced from the raw material cost as well as from cost of production, since the cost of production is being calculated for captive consumption meant for domestic production.

Similarly, in case of duty free material consumption under import against advance license or under any other scheme (being a kind of export benefit) landed cost shall be notionally adjusted by adding import duty content and the same shall be considered on par with duty paid material.

(c) **Bought out components:** Landed cost of indigenous / imported / bought out items shall be calculated on the above basis.

(d) **Self manufactured components:** These will include any goods manufactured with raw material, indigenous or imported bought out material etc. by the manufacturer in the same factory for further use in manufacture of final product. For this purpose the cost of production of such self manufactured items shall be considered as material cost for the subsequent product, after considering inward freight, octroi, etc., as applicable. Intermediate products, goods transferred by another unit of the same manufacturer etc. shall be based on cost of production + 10% (i. e. CAS – 4)

(e) **Process material, colour and chemicals, packing materials:** The cost of these shall be calculated on the same lines as above. In some cases, these items may be got manufactured on job work basis

from outside parties. In such cases, cost should consist of the cost of material supplied plus job work charges/processing charges paid to the job worker/processor. The incidental charges like freight, insurance, handling charges etc, if any shall also form cost of material.

In case of certain process materials like catalysts having longer process useful life, the cost of catalyst should be spread over entire production over the process useful life.

Reconciliation

1. **Quantitative reconciliation**- Input-output reconciliation of different types of major direct materials covering at least 80% of the total cost is necessary to ensure that quantity of material considered for calculating cost of production of captively consumed product is correct.

2. **Reconciliation of cost of material consumed**- It is advisable that cost of the material consumption considered for working out cost of production is reconciled with financial books.

5.2 Direct wages and salaries:

Direct wages and salaries shall include house rent allowance, overtime and incentive payments made to employees directly engaged in the manufacturing activities.

Direct wages and salaries include fringe benefits such as:

- (i) Contribution to provident fund and ESIS
- (ii) Bonus/ ex-gratia payment to employees
- (iii) Provision for retirement benefits such as gratuity and superannuation
- (iv) Medical benefits
- (v) Subsidised food
- (vi) Leave with pay and holiday payment
- (vii) Leave encashment

(viii) Other allowances such as children's education allowance, conveyance allowance which are payable to employees in the normal course of business etc.

Notes:

Employees cost can also be classified as direct employees cost and indirect employees cost. As per CAS 1

Direct wages and salaries mean the cost of wages, salaries of those workers / technicians who are readily identified or linked with a production cost centre or cost object.

Indirect employee cost is an employee cost which is not directly identifiable with the product or service as explained above.

As per CAS 1 direct employee cost shall include the fringe benefits like provident fund contribution, gratuity, ESI, overtime, incentives, bonus, ex-gratia, leave encashment, wages for holidays and idle time, etc.

Wages and salaries shall include HRA, Overtime and Incentive payments

Direct wages and salaries shall also include fringe benefits such as :

- (i) Contribution to provident fund and ESI.
- (ii) Bonus/ ex-gratia payment to employees.
- (iii) Provision for retirement benefits such as gratuity and superannuation
- (iv) Medical benefits
- (v) Subsidised food
- (vi) Leave with pay and Holiday payment.
- (vii) Leave encashment
- (viii) Other allowances such as children's education allowance, conveyance allowance, etc. which are payable to employees in the normal course of business.

While Direct Wages & Salaries is shown separately in the product cost sheet, the Indirect wages and salaries will form part of overheads in the respective cost centers.

VRS payment shall be treated as abnormal cost.

5.3 Direct Expenses

Direct expenses are the expenses other than direct material cost and direct employee's costs which can be identified with the product.

Direct expenses include:

- (i) Cost of utilities such as fuel, power, water, steam etc
- (ii) Royalty based on production
- (iii) Technical Assistance / know-how fees
- (iv) Amortized cost of moulds, patterns, patents etc
- (v) Job charges
- (vi) Hire charges for tools and equipment
- (vii) Charges for a particular product designing etc.

Notes:

Direct expenses include:

(i) Cost of utilities such as fuel, power (purchased as well as generated), water, steam etc : The actual cost of such utilities should be charged to various products manufactured, based on its usage for different products when they are directly identifiable with a product or service or production cost centre. In other cases, the same may be treated as indirect expenses forming part of works overheads.

(ii) Royalty based on production: If royalty payment is in respect of production of the goods captively consumed then the same should be added as the cost element. Royalty for (a) Upgrading Technology (b) Marketing and Distribution of products. For (a) Royalty will be included in cost of production, irrespective

of whether paid on production basis or sales basis. For (b) Royalty will be excluded from cost of production.

(iii) Technical Assistance/ know-how fees : Technical Assistance / know-how fees should be apportioned to products for which it is payable based on the payment / provision for the relevant period.

(iv) Amortized cost of moulds, dies, patterns, patents etc : The cost under this head should be apportioned to products for which such moulds, patterns, patents are used which are directly identifiable with the products, based on the useful life of the item.

(v) Job/processing charges: Job Work Charges / Processing Charges which are directly identified or linked with the products will form part of direct expenses.

(vi) Hire charges for tools and equipment: Hire charges in respect of tools and equipments which can be readily identified with a particular product will form part of direct expenses. Hire charges for tools and equipment for general use is in the nature of indirect expenses and is to be included in works overheads.

(vii) Charges for a particular product designing etc.: Product design charges to the extent amortized in respect of tools and equipments which can be directly identified with a particular product will form part of direct expenses.

5.4 Works Overheads:

Works overheads are the indirect costs incurred in the production process.

Works overheads include the following expenses:

- (i) Consumable stores and spares
- (ii) Depreciation of plant and machinery, factory building etc
- (iii) Lease rent of production assets
- (iv) Repair and maintenance of plant and machinery, factory building etc
- (v) Indirect employees cost connected with production activities
- (vi) Drawing and Designing department cost.
- (vii) Insurance of plant and machinery, factory building, stock of raw material & WIP etc
- (viii) Amortized cost of jigs, fixtures, tooling etc
- (ix) Service department cost such as Tool Room, Engineering & Maintenance, Pollution Control etc.

Notes:

The word overhead is used for a type of cost that cannot be directly allocated to a cost centre or product, but can only be apportioned to cost units. Overheads comprise of indirect materials, indirect employee costs and indirect expenses which are not directly identifiable or allocable to a cost object in an economically feasible way.

As per CAS-1, materials which are of small value and cannot be identified in or allocated to a product/service are classified as indirect material e.g., consumables, spare parts, lubricants etc.

Indirect employees cost is the cost of employees which are not directly allocable to a particular cost centre/object.

For the purpose of working out cost of production, classification of overheads according to function is necessary in order to ascertain the cost of each function.

The overheads are classified as:

- (i) Works overheads (also known as production overheads, factory overheads or manufacturing overheads)
- (ii) Administration Overheads relating to production activity
- (iii) Administration Overheads relating to post production activity
- (iv) Research and Development overheads
- (v) Selling overheads
- (vi) Distribution overheads.

All the above items of overheads except (iii), (v) and (vi) will be part of cost of production.

Cost Accounting Standard 3, which deals with the methods of collection, allocation, apportionment of overheads to different cost centres and absorption thereof to products or services, should be followed to maintain uniformity in respect of classification and allocation of overheads.

A reconciliation statement showing the amount incurred under different heads of overheads and amount absorbed by different products used for captive consumption and for sale should be prepared by the assessee. The reconciliation will help in ensuring accuracy of cost statements.

Depreciation : The depreciation on the fixed assets shall be as per the method of depreciation followed for the purpose of financial accounts.

Depreciation on idle fixed assets shall be excluded from cost of production.

The depreciation shall not be worked out on the basis of effective life of the asset. Further, depreciation should not be calculated based on the replacement value or notional value on revaluation of the assets.

Insurance premium for various assets and risk connected with production activity should be included in works overheads. However, insurance on loss of profit policy and finished goods in transit policy should not be part of works overhead.

Lease rental on fixed asset shall be also considered under this head.

5.5 Quality Control Cost:

The quality control cost is the expenses incurred relating to quality control activities for adhering to quality standard. These expenses shall include salaries & wages relating to employees engaged in quality control activity and other related expenses.

Notes:

Quality control cost shall include various costs related to Quality Control, Quality Assurance Department, Testing, Analysis Charges, Fees / Charges paid to IS / QS / Quality certification agencies.

5.6 Research and Development Cost

The research and development cost incurred for development and improvement of the process or the existing product shall be included in the cost of production.

Notes:

Research and Development cost is the cost of undertaking research to improve quality of the existing product or improve process of manufacture. The R & D cost for the existing product/process shall be included in the cost of production. In case the company has followed a policy to treat a part of the R&D cost of existing product/process as deferred cost, such share applicable for the year/period will be included in cost of production.

R & D cost incurred for developing a new product should be excluded from calculation of cost of production.

5.7 Administrative Overheads:

Administrative overheads need to be analyzed in relation to production activities and other activities. Administrative overheads in relation to production activities shall be included in the cost of production. Administrative overheads in relation to activities other than manufacturing activities e.g. marketing, projects management, corporate office expenses etc. shall be excluded from the cost of production.

Notes:

Administrative Overheads for production may include share from:

- Salaries of staff for administrative and other departments relating to production such as Accounts, Purchase, HRD, Production Planning.
- General office expenses - like rent, lighting, rates& taxes, telephone, stationery, postage etc.
- Depreciation of office building, office equipment, furniture, vehicles, etc
- Repairs & Maintenance of office building, office equipment, furniture, vehicles, etc.
- Legal expenses in relation to factory.

The role of administration is to facilitate the manufacturing, general policy making and marketing activities. The administrative overheads shall be included in the cost of production only to the extent they are attributable to the factory.

Administrative overheads in relation to activities other than manufacturing activities e.g. marketing, selling, depot/branches etc. shall be excluded from the cost of production.

Treatment of Head Office/Corporate Office Expenses:

Many a time, in a company, expenses of Head Office are booked separately. In a multi-locational multi-product company, there are common activities which are housed in corporate house called Head Office located away from the plants or in separate location in the complex of the plant. But it may so happen that certain activities common to all plants/products like purchase, inventory management, finance, personnel, R & D, Quality Assurance, etc., may be centralized at one place i.e. Head Office and booked as head office expenses along with other exclusive activities like secretarial, project, treasury, investment, trading, etc.

It is not correct that works and administration overheads shall include the cost of such departments only if they are situated in the factory premises

To fulfill the requirement that all 'administrative overheads in relation to production activities shall be included in the cost of production', it is necessary to properly segregate expenses of such activities of head office and follow suitable bases for allocating to plants/products on fair and equitable basis. In other words, it is suggested to open up different functional cost centres under head office and adopt suitable bases for apportioning share of expenses of relevant functional cost centres to plants/products for inclusion in the cost of production.

Freight and forwarding charges on dispatch of goods for captive consumption:

In case goods for captive consumption are dispatched from one factory premises to another factory premises, the cost of transportation incurred by sender of the goods is to be treated as cost of transportation under Rule 5 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, hence excluded from calculation of cost of production for CAS-4.

5.8 Packing cost

If product is transferred/dispatched duly packed for captive consumption, cost of such packing shall be included.

Packing cost includes both cost of primary and secondary packing required for transfer/ dispatch of the goods used for captive consumption.

Notes:

Packing Cost includes:

- (i) Cost of Packing Material
- (ii) Job charges paid for manufacture of packing material. if any.
- (iii) Packing charges including salaries & wages of the persons involved in packing activity.
- (iv) Other expenses relating to packing activity.

Landed cost of the packing material should be calculated as per the guidelines given in para related to material cost.

If product for captive consumption is transferred without packing (unpacked), packing cost need not be included in the cost of production. In case captive product is transferred on returnable/durable packing container, pro-rata cost shall be estimated and charged based on the life of the container.

5.9 Absorption of overheads:

Overheads shall be analysed into variable overheads and fixed overheads.

Variable Overheads are the items which change with the change in volume of production, such as cost of utilities etc.

Fixed overheads are the items whose value do not change with the change in volume of production such as staff salaries, rent etc.

The fixed production overheads and other similar items of fixed costs such as quality control cost, research and development costs, administrative overheads relating to manufacturing shall be absorbed in the production cost on the basis of the normal capacity or actual capacity utilization of the plant, whichever is higher.

Notes:

Absorption of overheads and calculation of cost of production: Variable Overheads comprise of expenses which vary in proportion to the change in the volume of production e.g. variable portion of salaries and wages, cost of utilities, royalty, job charges, etc.

Fixed overheads comprise of expenses which do not vary with the change in volume of production such as fixed portion of salaries and wages, rent, insurance, technical assistance/know-how fees, amortized cost of moulds, patterns, patents, hire charges for tools and equipments, charges for a particular design, various items of works overheads listed in para 5.4, quality control and R & D, etc.

The principles laid down in CAS-3, which deals with the methods of collection, allocation, apportionment of overheads to different cost centers and absorption thereof to products or services on a consistent and uniform basis in the preparation of cost statements should be followed for the purpose of allocation and absorption of overheads.

The variable production overheads shall be absorbed in cost of product, based on actual capacity utilisation.

When the plant is producing or utilizing capacity below normal capacity, the absorption of fixed production overheads should be done on normal capacity irrespective of actual capacity utilised.

It is advisable that a reconciliation statement showing the amount incurred under different heads of overheads and amount absorbed by different products should be prepared for this purpose. The reconciliation will help in ensuring accuracy of cost of production in cost statements.

5.10 Valuation of Stock of work-in-progress and finished goods

Stock of work-in-progress shall be valued at cost on the basis of stages of completion as per the cost accounting principles. Similarly, stock of finished goods shall be valued at cost. Opening and closing stock of work-in-progress shall be adjusted for calculation of cost of goods produced and similarly opening and closing stock of finished goods shall be adjusted for calculation of goods dispatched.

In case the cost of a shorter period is to be determined, where the figures of opening and closing stock are not readily available, the adjustment of figures of opening and closing stock may be ignored.

Notes:

The Excise Duty is payable at the time of removal of goods, therefore, cost of production is to be calculated for quantity dispatched. This will necessitate adjustment of cost of opening and closing stock of finished goods from cost of production of quantity produced.

In case of companies registered under the Companies Act, 1956, the valuation of inventory, (Raw Material, WIP and Finished Goods) is based on AS-2 of ICAI. However, for calculation of cost of

production for CAS-4 certificate, the valuation of inventory shall be as per the method of costing as explained above, which may not be same as per AS-2.

In case the product costing is required to be worked out for a new product i.e. for the future period, it will be done based on projected production, projected capacity utilisation and other parameters. In such cases valuation of opening stock and closing stock of WIP and Finished goods need not be considered.

In another situation, when the cost of production is to be worked out for the previous period then due consideration should be given for opening and closing stock of WIP and Finished goods.

5.11 Treatment of Joint Products and By-Products

A production process may result in more than one product being produced simultaneously. In case joint products are produced, joint costs are allocated between the products on a rational and consistent basis. In case by-products are produced, the net realisable value of by-products is credited to the cost of production of the main product.

For allocation of joint cost to joint products, the sales values of products at the split off point i.e. when the products become separately identifiable may become the basis. Some other basis may be adopted. For example, in case of petroleum products, each product is assigned certain value based on its certain properties, may be calorific value and these values become the basis of apportionment of joint cost among petroleum products.

Notes:

The cost of production of Joint Products can be worked out as per the generally accepted cost accounting principles. However, it is not possible to calculate the cost of production of by-products.

5.12 Treatment of Scrap and Waste:

The production process may generate scrap or waste. Realized or realizable value of scrap or waste shall be credited to the cost of production.

In case, scrap or waste does not have ready market and it is used for reprocessing, the scrap or waste value shall be taken at a rate of input cost depending upon the stage at which such scrap or waste is recycled. The expenses incurred for making the scrap suitable for reprocessing shall be deducted from value of scrap or waste.

Normal process loss is ignored for the sake of simplicity.

If the cost calculation is done for the past period and if the actual sales realization of scrap is available, then the same shall be deducted after adjustment for opening and closing stock of scrap (to arrive at the realisable value of scrap generated) from the cost of production for the relevant period.

In case the scrap is not disposed off/sold during the period and lying in the stock, the realizable value of scrap can be calculated from the quotations/market rate.

It is not possible to calculate cost of production of scrap and waste.

5.13 Miscellaneous Income:

Miscellaneous income relating to production shall be adjusted in the calculation of cost of production, for example income from sale of empty containers used for dispatch of the captively consumed goods produced under reference.

Notes:

The miscellaneous income needs to be analysed carefully for its nature and only if the same is not related to production activities, the same may be ignored.

The phrase “used for dispatch of the captively consumed goods produced under reference” shall be ignored. The income arising out of sale of used empty containers of the input materials shall be adjusted in the cost of production.

5.14 Inputs received free of cost

In case any input material, whether of direct or indirect nature, including packing material is supplied free of cost by the user of the captive product, the landed cost of such material shall be included in the cost of production.

Notes:

Landed cost of inputs received free of cost should be calculated as per the guidelines given in para related to material cost.

5.15 Moulds, Tools, Dies & Patterns etc received free of cost:

The amortization cost of such items shall be included in the cost of production.

Notes: Amortisation should be done on the basis of estimated production that can be achieved during the life of the Mould, Tool, Die or Pattern. After the estimated life, if the moulds, dies are still in use and if the full cost has already been amortised, then amortisation cost need not be considered for the purpose of cost of production. However, for this purpose, proper record needs to be maintained. The estimated life / estimated production may be certified by technical person. Where the dies, moulds etc are supplied by the customer, the necessary details may be obtained from the customer.

In case of dies, moulds etc purchased / manufactured in-house same principles shall be adopted.

5.16 Interest and financial charges:

Interest and financial charges being a financial charge shall not be considered to be a part of cost of production.

Notes:

Interest and financial charges are finance cost, hence shall not be considered as a part of cost of production. Interest will be net of interest income and cash discount received. Financial charges will cover items like L/C charges, bank charges and guarantee commission.

5.17 Abnormal and non-recurring cost

Abnormal and non-recurring cost arises due to unusual or unexpected occurrence of events, such as heavy break down of plants, accident, market condition restricting sales below normal level, abnormal idle capacity, abnormal process loss, abnormal scrap and wastage, payments like VRS, retrenchment compensation, lay-off wages etc. The abnormal cost shall not form the part of cost of production.

Notes:

In addition to the above events, cost of trial run for production and loss due to fire and natural calamities shall also be treated as abnormal and non-recurring cost, hence omitted from cost of production. Further, expenses which are not related to manufacturing activity and which do not form part of the cost as per the generally accepted cost accounting principles may be ignored for this purpose e.g. - donations, loss on sale of fixed assets, etc.

6. Cost Sheet:

The cost sheet should be prepared in the format as per Appendix-1 or as near thereto as possible. The manufacturer will be required to maintain cost records and other books of account in a manner, which would facilitate preparation and verification of the cost of production. For manufacturers covered under the ambit of Section 209(1)(d) of the Companies Act, 1956, Le., where Cost Accounting Records are statutorily required to be maintained, the Cost Accountant certifying the cost of production for captive consumption shall verify the correctness of the cost from these records. However, for manufacturers not covered under Section 209(1)(d) of the Companies Act, 1956, it is desirable that they also maintain cost accounting records in line with the records so prescribed so as to facilitate determination and certification of cost of production.

Notes: Separate cost sheet shall be prepared for each type/ variety/description of product used for captive consumption. The cost sheet may be suitably modified to cover the special features, if any, of the industry. The Cost Accountant certifying the cost of production statement shall verify and reconcile the product cost arrived at for the certification with that worked out to comply with provisions of Section 209(1)(d) of the Companies Act, 1956.

7. Disclosure:

(i) If there is any change in cost accounting principles and practices during the concerned period which may materially affect the cost of production in terms of comparability with previous periods, the same should be disclosed.

(ii) If opening stock and closing stock of work -in-progress and finished goods are not readily available for certification purpose, the same should be disclosed.

Notes:

Disclosure shall be made by way of “Notes to Certificate” below the certificate.

8.FAQ issued by the Institute of Cost Accountants of India

Q.1: What is the objective of Cost Accounting Standard on Cost of production for Captive Consumption (CAS -4)?

Answer: The Institute of Cost Accountants of India released Cost Accounting Standard on Cost of production for Captive Consumption (CAS - 4) on 13rd January 2003, with a view to bring uniformity in the principles and methods used for determining the cost of production of excisable goods used for captive consumption for the purposes of Rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000.

Q.2: Whether the Cost of Production of captively consumed goods is to be calculated as per CAS 1, CAS 2, CAS 3 and CAS 4 issued by the Institute?

Answer: Rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 requires determination of cost of production or manufacture where the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles. CAS-4 defines the methodology of cost determination for this purpose and imbibes the principles postulated in CAS 1, CAS 2 and CAS 3 which are general principles of costing.

Note: The words “where the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles” were amended and replaced by words “Where whole or part of the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles “ by Notification NO. 14 / 2013 dated 22nd November, 2013.

Q.3: How Cost of Production of captively consumed goods is to be calculated?

Answer: CAS-4 stipulates that Cost of Production of captively consumed goods shall consist of material consumed, direct wages and salaries, direct expenses, works overheads, quality control cost, research and development cost, packing cost, administrative overheads relating to production and to arrive at the cost of production for captive consumption, adjustment for stock of work-in-progress, finished goods, recoveries for sales of scrap, wastage etc. are to be carried out. It further stipulates that the fixed production overheads and other similar item of fixed costs such as quality control cost, research and development costs, and administrative overheads relating to manufacturing shall be absorbed in the production cost on the basis of the normal capacity or actual capacity utilization of the plant, whichever is higher. The cost accounts for this purpose shall be reconciled with the audited financial accounts.

Q.4: Whether the Cost of Production is to be calculated separately for each production unit or the Company as a whole?

Answer: In case of Multi location units, the Cost of Production is to be determined separately for each unit and not for the Company as a whole.

Q.5: What is the periodicity of CAS - 4 Certification?

Answer: Cost determination of a product is always for a period and computed on the basis of actual accounts of the company. The CBEC circular no. M.F.(D.R.) F.No. 354/81/2000-TRU, dated 30-6-2000 also envisages to value goods which are captively consumed on cost construction method. Further, costs so determined should be actual cost reconciled with the audited accounts of the company to ensure correctness. In any case, the actual cost for a period can only be available after the accounts for the period is audited. Consequently, it is contemplated that the cost of production certification under CAS-4 be done half-yearly and goods cleared. The company would be provisionally assessed under rule 7 of Central Excise Rules, 2002. After the end of the year and annual certification under CAS-4 on the basis of audited annual accounts, differential duty, if any, shall be paid by the company.

Q 6: Is a certificate issued under CAS – 4 by any professional other than a Cost Accountant in Practice valid or not?

Answer: No, the certificate has to be issued by a Cost Accountant in practice only.

Q.7: Which year's cost of production would be relevant for CAS - 4?

Answer: The Cost of production has to be the relevant year's average cost of production.

Q.8: Is the cost of production required to be determined for different varieties, sizes separately?

Answer: In case the company is manufacturing and consuming the goods in different varieties and/or sizes etc., the cost of production for each of the variety / size should be worked out separately

Q.9: Is CAS - 4 applicable to manufacturers falling in the category of proprietorship, partnership, co-operative sector, SSI Units?

Answer: Yes. CAS-4 is applicable to all entities who are liable to pay excise duty and is clearing goods under Rule 8 of the Central Excise Valuation Rules for the purpose of captive consumption of such goods, irrespective of the constitution of the entity.

Q.10: Whether all items of Profit & Loss Account, are to be considered while determining the Cost of Production as per CAS - 4?

Answer: Profit & Loss Account represents the true and fair view of profit for a period and is derived on the basis of financial accounts of a company consisting of various items of incomes and expenses considered in accordance with the relevant accounting standards. Cost accounting, on the other hand consists of items of costs classified according to its nature and incidence which are allocated and apportioned to products on the basis of cost accounting standards and generally accepted cost accounting principles to arrive at the cost of production. CAS-4, which defines the cost components to be considered to arrive at cost of production for captive consumption has defined the various items of cost

components to be considered for the purpose and the resultant cost is required to be reconciled with the audited Profit & Loss Account to ensure that all items of costs are considered in the cost construction and such items of expenses or incomes which do not form part of cost of production are properly dealt with in the reconciliation between the cost accounts and financial accounts. For example, Loss on sale of fixed assets, bad debts written off, unabsorbed overheads due to under-utilization of capacity, abnormal costs, Loss/Gain on foreign exchange transactions, miscellaneous incomes not related to the product or production activity etc. do not form part of cost of production though these would appear in the Profit & Loss Account. Further, expenses relating to selling and distribution or corporate overheads will also not form part of Cost of production though expenses comprised in such overheads would be a part of the Profit & Loss Account. However, such other operating incomes, e.g., sale of scrap, sale of used empty containers of the input material would be considered as a credit to the Cost of Production.

Q.11: What is the treatment of overheads for working out the Cost of Production, under CAS - 4?

Answer: The variable production overheads are to be absorbed based on actual capacity utilisation and the fixed production overheads are to be absorbed on Normal Capacity or Actual Capacity Utilisation, whichever is higher. In case Actual Capacity Utilisation is lower than the Normal Capacity, the absorption of Fixed Overheads should be done on normal capacity irrespective of Actual Capacity Utilised.

Q.12: Whether any inputs received free of cost shall be included in the Cost of Production under CAS – 4 or not?

Answer: Landed Cost of input material received free of cost shall be included in the Cost of Production for Captive Consumption for the purpose of determination of value as contemplated in Rule 8.

Q.13: When the goods produced are used by the assesses in the production or manufacture of other articles in the same premises or elsewhere, is the Cost of Production required to be calculated as per CAS – 4 and assessable value 110% thereof?

Answer: As per Rule 8 of the Central Excise Valuation Rules, where the excisable goods are not sold but are used for consumption by the assesses or on his behalf in the production or manufacture of other articles, the assessable value shall be 110% of Cost of Production unless exempted and the Cost of Production is to be calculated as per CAS - 4.

Q.14. Whether Interest and Finance charges are to be included while working out the Cost of production?

Answer: Interest and finance charges do not form part of Cost of Production for Captive Consumption. As per the Valuation Rules, the assessable value is considered to be 110% of the cost of production determined in accordance with CAS-4.

9. Opinions from the Technical Cell of the Cost Accounting Standards Board (CASB)

1. Costing of parts of Motor vehicles manufactured and sold to related unit.

Tech/CASB/2011/12

Date: 13th December 2011

Shri John Joseph

Commissioner, Large Taxpayer Unit
Central Excise and Service Tax, LTU
NBCC Plaza, Pushp Vihar, Saket,
New Delhi – 110017
Dear Sir,

Subject: Costing of parts of Motor vehicles manufactured and sold to related unit.

This has reference to your letter no C.No.LTU/CEX/Adj/ITL/282/2011 dated 22.11.2011 to our Institute seeking its comments / views regarding costing of parts of motor vehicles manufactured and sold to related units by International Tractors Limited, Hoshiarpur – in particular, the compliance with cost accounting standards CAS 1 to 4 .The Technical Cell of the Cost Accounting Standard Board of the ICWAI considered the above referred matter at its meeting held on 9th December 2011 and the undersigned is pleased to forward the option of the Technical Cell as below.

Brief Facts of the case

We note that International Tractors Limited is a manufacturer of MUV Engines and sheet metal parts of motor vehicles in addition to tractors. The sale of sheet metal parts and MUV engines to a related unit are being assessed to excise on the basis of 110% of cost of production. We also note that while arriving at the cost of production, the company has considered actual material cost and allocated others cost on the basis of installed capacity. It is further noted that the company never achieved the installed capacity during the period of 5 years ending with 2009-10.

It is also noted that while arriving at the cost of goods sold, the department has considered the actual production of goods as the basis of allocation of costs. It is noted that there is no dispute regarding valuation of cost of material consumption, which has been done at the actual material cost.

Comments

The Institute has relied upon the following cost accounting standards to arrive at the option for issue under reference.

CAS-4 dealing with the determination of cost of production for captive consumption is applicable to the present case. The Standard refers to the capacity utilization in the context of absorption of overheads. The standard explicitly states that:

- Variable overheads shall be absorbed in production cost based on actual capacity utilization.
- Fixed production overheads and other similar items of fixed cost such as quality control cost, R&D cost and administration overheads relating to manufacturing shall be absorbed on the basis of normal capacity or actual capacity utilization, whichever is higher.

CAS-4 [Para 4.3] defines Normal Capacity as “Normal Capacity is the production achieved or achievable on an average over a period or season under normal circumstances taking into account the loss of capacity resulting from planned maintenance.”

A constructive reading of the above would show that installed capacity cannot be considered for allocation of fixed overheads.

At the same time, actual production cannot also be considered for allocation of fixed overheads, which should be absorbed on normal capacity unless the actual production is higher than the normal capacity.

Conclusion:

- a) Valuation of cost of production for captive consumption is to be done in accordance with the procedure laid down in CAS-4.
- b) Actual material Cost is to be considered for determination of cost of production.
- c) Variable Overheads is to be absorbed in cost of production on the basis of actual production.
- d) Fixed production overheads and other similar items of fixed costs such as quality control cost, research and development cost and administration overheads relating to manufacturing are to be absorbed in the production cost based on normal capacity or actual capacity utilization whichever is higher.

We trust our comments and views are helpful in applying the standards to the case in points. Should you require any further clarification, please feel free to write to us.

Yours faithfully,

J.P. Singh
Director (Technical) and
Secretary, Cost Accounting Standards Board of ICWAI

ANNEXURE-A

(CAS-4)

COST ACCOUNTING STANDARD ON

COST OF PRODUCTION FOR CAPTIVE CONSUMPTION

The following is the text of the COST ACCOUNTING STANDARD 4 (CAS-4) issued by the Council of the Institute of Cost and Works Accountants of India on "Cost of Production for Captive Consumption". The standard deals with determination of cost of production for captive consumption. In this Standard, the standard portions have been set in bold italic type. These should be read in the context of the background material which has been set in normal type.

1. Introduction

The Cost Accounting principle for determination of cost of production is well established. Similarly, rules for levy of excise duty on goods used for captive consumption are also well defined. Captive Consumption means the consumption of goods manufactured by one division and consumed by another division(s) of the same organization or related undertaking for manufacturing another product(s). Liability of excise duty arises as soon as the goods covered under excise duty are manufactured but excise duty is collected at the time of removal or clearance from the place of manufacture even if such removal does not amount to sale. Assessable value of goods used for captive consumption is based on cost of production. According to the Central Excise Valuation (Determination of Price of Excisable Goods) Rules 2000, the assessable value of goods used for captive consumption is 115% of cost of production of such goods, and as may be prescribed by the Government from time to time.

2. Objective

- 2.1 The purpose of this standard is to bring uniformity in the principles and methods used for determining the cost of production of excisable goods used for captive consumption.
- 2.2 The cost statement prepared based on standard will be used for determination of assessable value of excisable goods used for captive consumption.
- 2.3 The standard and its disclosure requirement will provide better transparency in the valuation of excisable goods used for captive consumption.

3. Scope

- 3.1 The standard is to be followed for determining the cost of production to arrive at an assessable value of excisable goods used for captive consumption.
- 3.2 Cost of production will include various cost components. They are already defined in Cost Accounting Standard-1 ('Classification of Cost'- CAS-1). Thus, this standard has to be read in conjunction with CAS-1.

4. Definitions

4.1 Cost of Production : Cost of production shall consist of Material Consumed, Direct Wages and Salaries, Direct Expenses, Works Overheads, Quality Control cost, Research and Development Cost , Packing cost, Administrative Overhead s relating to production.

To arrive at cost of production of goods dispatched for captive consumption, adjustment for Stock of work-in-Process, finished goods, recoveries for sales of scrap, wastage etc shall be made.

4.2 Captive Consumption : Captive Consumption means the consumption of goods manufactured by one division or unit and consumed by another division or unit of the same organization or related undertaking for manufacturing another product(s).

4.3 Normal Capacity is the production achieved or achievable on an average over a period or season under normal circumstances taking into account the loss of capacity resulting from planned maintenance. (CAS-2)

5. Determination of Cost of Production for Captive Consumption

To determine the cost of production for captive consumption, calculations of different cost components and adjustments are explained below :

5.1 Material Consumed

Material Consumed shall include materials directly identified for production of goods such as :

- a) *indigenous materials*
- b) *imported materials*
- c) *bought out items*
- d) *self manufactured items*
- e) *process materials and other items*

Cost of material consumed shall consist of cost of material, duties and taxes, freight inwards, insurance, and other expenditure directly attributable to procurement. Trade discount, rebates and other similar items will be deducted for determining the cost of materials. Cenvat credit, credit for countervailing customs duty, Sales Tax set off, VAT, duty draw back and other similar duties subsequently recovered / recoverable by the enterprise shall also be deducted.

5.2 Direct wages and salaries

Direct wages and salaries shall include house rent allowance, overtime and incentive payments made to employees directly engaged in the manufacturing activities.

Direct wages and salaries include fringe benefits such as:

- (i) Contribution to provident fund and ESIS
- (ii) Bonus/ ex-gratia payment to employees
- (iii) Provision for retirement benefits such as gratuity and superannuation

- (iv) Medical benefits
- (v) Subsidised food
- (vi) Leave with pay and holiday payment
- (vii) Leave encashment
- (viii) Other allowances such as children's education allowance, conveyance allowance which are payable to employees in the normal course of business etc.

5.3 Direct Expenses

Direct expenses are the expenses other than direct material cost and direct employee's costs which can be identified with the product.

Direct expenses include:

- (i) Cost of utilities such as fuel, power, water, steam etc
- (ii) Royalty based on production
- (iii) Technical Assistance / know-how fees
- (iv) Amortized cost of moulds, patterns, patents etc
- (v) Job charges
- (vi) Hire charges for tools and equipment
- (vii) Charges for a particular product designing etc.

5.4 Works Overheads

Works overheads are the indirect costs incurred in the production process.

Works overheads include the following expenses:

- (i) Consumable stores and spares
- (ii) Depreciation of plant and machinery, factory building etc
- (iii) Lease rent of production assets
- (iv) Repair and maintenance of plant and machinery, factory building etc
- (v) Indirect employees cost connected with production activities
- (vi) Drawing and Designing department cost.
- (vii) Insurance of plant and machinery, factory building, stock of raw material & WIP etc
- (viii) Amortized cost of jigs, fixtures, tooling etc
- (ix) Service department cost such as Tool Room, Engineering & Maintenance, Pollution Control etc

5.5 Quality Control Cost

The quality control cost is the expenses incurred relating to quality control activities for adhering to quality standard. These expenses shall include salaries & wages relating to employees engaged in quality control activity and other related expenses.

5.6 Research and Development Cost

The research and development cost incurred for development and improvement of the process or the existing product shall be included in the cost of production.

5.7 Administrative Overheads

Administrative overheads need to be analysed in relation to production activities and other activities. Administrative overheads in relation to production activities shall be included in the cost of production. Administrative overheads in relation to activities other than manufacturing activities e.g. marketing, projects management, corporate office expenses etc. shall be excluded from the cost of production.

5.8 Packing Cost

If product is transferred/dispached duly packed for captive consumption, cost of such packing shall be included.

Packing cost includes both cost of primary and secondary packing required for transfer/ dispatch of the goods used for captive consumption.

5.9 Absorption of overheads

Overheads shall be analysed into variable overheads and fixed overheads.

Variable Overheads are the items which change with the change in volume of production, such as cost of utilities etc.

Fixed over heads are the items whose values do not change with the change in volume of production such as salaries, rent etc.

The variable production overheads shall be absorbed in production cost based on actual capacity utilisation.

The fixed production overheads and other similar item of fixed costs such as quality control cost, research and development costs, administrative overheads relating to manufacturing shall be absorbed in the production cost on the basis of the normal capacity or actual capacity utilization of the plant, whichever is higher.

5.10 Valuation of Stock of work-in-progress and finished goods

Stock of work-in-progress shall be valued at cost on the basis of stages of completion as per the cost accounting principles. Similarly, stock of finished goods shall be valued at cost. Opening and closing stock of work-in-progress shall be adjusted for calculation of cost of goods produced and similarly opening and closing stock of finished goods shall be adjusted for calculation of goods despatched.

In case the cost of a shorter period is to be determined, where the figures of opening and closing stock are not readily available, the adjustment of figures of opening and closing stock may be ignored.

5.11 Treatment of Joint Products and By-Products

A production process may result in more than one product being produced simultaneously. In case joint products are produced, joint costs are allocated between the products on a rational and consistent basis. In case by-products are produced, the net realisable value of by-products is credited to the cost of production of the main product.

For allocation of joint cost to joint products, the sales values of products at the split off point i.e. when the products become separately identifiable may become the basis. Some other basis may be adopted. For example, in case of petroleum products, each product is assigned certain value based on its certain properties, may be calorific value and these values become the basis of apportionment of joint cost among petroleum products.

5.12 Treatment of Scrap and Waste

The production process may generate scrap or waste. Realized or realizable value of scrap or waste shall be credited to the cost of production.

In case, scrap or waste does not have ready market and it is used for reprocessing, the scrap or waste value is taken at a rate of input cost depending upon the stage at which such scrap or waste is recycled. The expenses incurred for making the scrap suitable for reprocessing shall be deducted from value of scrap or waste.

Illustration

A production process has three stages.

<u>Stage</u>	<u>Input material cost</u>	<u>Processing cost</u>	<u>Total</u>
	(Rs/ MT)	(Rs/MT)	(Rs/MT)
1	2000	500	2500
2	2500	1000	3500
3	3500	1000	4500

If during the production process at stage3, the scrap is produced and the same is recycled at stage2 after making an expenditure of Rs 200 per MT to make it suitable for re-processing at stage2, then scrap will be valued @ Rs (2500 – 200) i.e. Rs 2300.If no expenditure is involved to make scrap re-usable, the scrap value will be @ Rs 2500. The scrap value for the scrap produced during a period calculated at the rate as explained above may be deducted to find out the cost of production for the period.

5.13 Miscellaneous Income

Miscellaneous income relating to production shall be adjusted in the calculation of cost of production, for example, income from sale of empty containers used for dispatch of the captively consumed goods produced under reference.

5.14 Inputs received free of cost

In case any input material, whether of direct or indirect nature, including packing material is supplied free of cost by the user of the captive product, the landed cost of such material shall be included in the cost of production.

5.15 Moulds, Tools, Dies & Patterns etc received free of cost

The amortization cost of such items shall be included in the cost of production.

5.16 Interest and financial charges

Interest and financial charges being a financial charge shall not be considered to be apart of cost of production.

5.17 Abnormal and non- recurring cost

Abnormal and non-recurring cost arising due to unusual or unexpected occurrence of events, such as heavy break down of plants, accident, market condition restricting sales below normal level, abnormal idle capacity, abnormal process loss, abnormal scrap and wastage, payments like VRS, retrenchment compensation, lay-off wages etc. The abnormal cost shall not form the part of cost of production.

6. Cost Sheet

The cost sheet should be prepared in the format as par Appendix – 1 or as near thereto as possible. The manufacturer will be required to maintain cost records and other books of account in a manner, which would facilitate preparation and verification of the cost of production. For manufacturers covered under the ambit of Section 209(1)(d) of the Companies Act, 1956, i.e., where Cost Accounting Records are statutorily required to be maintained, the Cost Accountant certifying the cost of production for captive consumption shall verify the correctness of the cost from these records. However, for manufacturers not covered under Section 209(1)(d) of the Companies Act, 1956, it is desirable that they also maintain cost accounting records in line with the records so prescribed as to facilitate determination and certification of cost of production.

7. Disclosure

(i) If there is any change in cost accounting principles and practices during the concerned period which may materially affect the cost of production in terms of comparability with previous periods, the same should be disclosed.

(ii) If opening stock and closing stock of work -in-progress and finished goods are not readily available for certification purpose, the same should be disclosed.

Appendix – 1

Name of the Manufacturer :

Address of the Manufacturer:

Registration No of Manufacturer:

Description of product captively consumed:

Excise Tariff Heading:

Statement of Cost of Production of _____ manufactured / to be manufactured during the period

		Qty	
Q 1	Quantity Produced (Unit of Measure)		
Q 2	Quantity Despatched (Unit of Measure)		
	Particulars	Total Cost (Rs)	Cost/Unit (Rs)
1.	Material Consumed		
2.	Direct Wages and Salaries		
3.	Direct Expenses		
4.	Works Overheads		
5.	Quality Control Cost		
6.	Research & Development Cost		
7.	Administrative Overheads (relating to production activity)		
8.	Total (1 to 7)		
9.	Add : Opening stock of Work - in –Progress		
10.	Less : Closing stock of Work -in- Progress		
11.	Total (8+9-10)		
12.	Less : Credit for Recoveries/Scrap/By-Products / misc income		
13.	Packing cost		
14.	Cost of production (11 - 12 + 13)		
15.	Add: Inputs received free of cost		
16.	Add: Amortised cost of Moulds, Tools, Dies & Patterns etc received free of cost		
17.	Cost of Production for goods produced for captive consumption(14 + 15 + 16)		
18.	Add : Opening stock of finished goods		
19.	Less : Closing stock of finished goods		
20.	Cost of production for goods despatched (17 + 18 - 19)		

Seal & Signature of Company's Authorised Representative

I/We, have verified above data on test check basis with reference to the books of account, cost accounting records and other records. Based on the information and explanations given to me/us, and on the basis of generally accepted cost accounting principles and practices followed by the industry, I /We certify that the above cost data reflect true and fair view of the cost of production.

Date :

Seal & Signature of Cost Accountant

Place :

Membership No.

ANNEXURE-B

Circular No.643/34/2002-CX.
1st July, 2002

F.NO. 6/39/2000 – CX 1
Government Of India
Ministry Of Finance
Department Of Revenue
Central Board Of Excise & Customs

Subject : Clarification of doubts under the new Valuation Rules

I am directed to refer to Board's letter F.No.354/81/2000-TRU dated 30th June 2000 clarifying certain points relating to the new valuation provisions made effective from 1.7.2000.

2. The Board has received a number of references from the field formations as well as representations from the trade associations about certain doubts still persisting in the minds of the field officers. These points of doubt are being clarified in the Table enclosed.

3. Field formations may be suitably informed.

4. Hindi version will follow

5. Receipt of this Circular may kindly be acknowledged.

Sd/-
(A.K.PRASAD)
DIRECTOR (CX I)
3092812

Clarifications on points of doubt under The New Valuation Provisions introduced w.e.f. 1.7.2000

Sl no.	Points of doubt	Clarification
1.	What is the scope of the term "greatest aggregate quantity" used in Rule 2(b) of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. The definition does not indicate the time period over which the quantity is to be computed. Further, it is not clear whether it refers to the largest quantity sold to any particular assessee during the period or to the goods sold to the largest number of buyers.	The term "greatest aggregate quantity" has been used to define the term "normal transaction value" used in Rules 7 and 9 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. Seen in this context the time period should be taken as the whole day and the transaction value of the "greatest aggregate quantity" would refer to the price at which the largest quantity of identical goods are sold on a particular day, irrespective of the number of buyers. In case the "normal transaction value" from the depot or other place is not ascertainable on the day identical goods are being removed from the factory/warehouse,

		the nearest day when clearances of the goods were affected from the depot or other place should be taken into consideration.
2.	Freight charges:- - How is the cost of transportation to be deducted in case of vehicles owned by the manufacturer ? - If manufacturer/transporter charges cost of transportation both for outward journey up to the point of delivery and return therefrom, whether the cost of transportation for the return journey of the empty truck/vehicle should also be allowed as deduction ? - Whether transit insurance can be allowed as deduction as being part of transportation cost?	(a) In such cases the cost of transportation can be calculated through costing method following the accepted principles of costing. A cost certificate from a certified Cost Accountant/Chartered Accountant/Company Secretary, may be accepted. The cost of transportation should, however, be separately shown in the invoice. (b) As per Rule 5 of the Valuation Rules the actual cost of transportation from the place of removal up to the place of delivery is only to be excluded. If the assessee is recovering an amount from the buyer towards the cost of return fare of the empty vehicle from the place of delivery, this amount will not be available as a deduction. If, however, only the cost of transportation has been indicated in the invoice without any breakup for the forward and return journey, normally it should be accepted as the cost of transportation from the place of removal to the place of delivery. (c) Yes, the Apex Court in the case of Bombay Tyres International has held that the cost of transportation will include the cost of insurance also during the transportation of the goods. But the transit insurance should either be shown separately in the invoice or can be included in the transportation cost shown separately.
3.	(a) Whether abatement of sales tax and other taxes can be allowed based on average tax actually paid by the assessee as supported by costing certificate? [Circular No 20/90 CX 1 dt 30.8.1990] (b) As per Board's Circular No.2/94-CX.1 dt.11.1.94 (F.No.6/20/94-CX.1) the sales tax set-off available in respect of inputs is to be ignored while computing the sales tax payable. Whether this is still valid?	- No. As per definition of "transaction value" taxes are deductible only on actual basis either paid or payable by the assessee. Attention is invited to paras 10 and 11 of Board's letter F.No.354/81/2000-TRU dt 30.6.2000. - No. The Circular dt.11th Jan.1994 was based on the definition of 'duty of excise payable' given in Explanation to the erstwhile Sec.4(4)(d)(ii). The new sec.4 does not incorporate any such Explanation. The "transaction value" will exclude the sales tax actually paid or payable on the goods. Thus, for example, if the effective sales tax on cum-duty price of Rs.100 is 4% and the assessee is eligible for set-off of sales tax of, say, Rs.10 paid/suffered on the inputs, the actual sales tax paid/payable would be Rs.40-10 = Rs.30 and this will be the amount permissible as deduction

		from the "transaction value" and not Rs 40/-. Attention is also invited to paras 10 and 11 of Board's letter F.No.354/81/2000- TRU dt 30.6.2000.
4.	Packing:- a. whether cost of secondary packing is to be excluded from the transaction value ? b. How is the cost of reusable containers to be determined for inclusion in the transaction value? c. Whether rental charges or cost of maintenance of reusable metal containers like gas cylinders etc. are to be included in the transaction value? d. What about cost of containers supplied by the buyer?	(a) No. There is no provision for such a deduction in the concept of transaction value (b) Normally the cost of reusable containers (glass bottles, crates etc.) is amortized and included in the cost of the product itself. Therefore the question of adding any further amount towards this account does not arise, except where Audit of accounts reveals that the cost of the reusable container has not been amortised and included in the value of the product (c) Yes, since the amount has been charged by reason of, or in connection with the sale of goods, this amount will be added to the transaction value (d) Since in such cases the price will not be the sole consideration for the sale, the valuation would be governed by Rule 6 and the cost of such packing, whether durable or not, will be included in the transaction value of the goods. In respect of packing which can be used repeatedly the cost will have to be amortized over the life span of the packing material as is done in the case of dies, moulds etc. supplied by the buyer.
5.	How will valuation be done in cases of captive consumption (i.e consumed within the same factory) including transfer to a sister unit or another factory of the same company/firm for further use in the manufacture of goods?	For captive consumption in one's own factory, valuation would be done as per rule 8 of the Valuation Rules i.e. the assessable value will be 115% of the "cost of production" of the goods. If the same goods are partly sold by the assessee and partly consumed captively, the goods sold would be assessed on the basis of "transaction value" [provided they meet the conditions of sec.4(1)(a)] and the goods captively consumed would be valued as per Rule 8 of the Valuation Rules. This is because, as per new section 4, transaction value has to be determined for each removal. Where goods are transferred to a sister unit or another unit of the same company valuation will be done as per the proviso to rule 9.
6.	Whether advertisement and publicity charges borne by the dealers/buyers are to be excluded from the assessable value	No. Even where the dealings are on principal to principal basis but there is an agreement either written or oral that the buyer will incur certain expenditure for advertising the goods of the assessee, the cost of such advertisement and publicity will be added to the price of the goods to determine the assessable value. In such cases since price would not be sole consideration for sale, the transaction value

		would be covered by Rule 6 of the Valuation Rules As per definition, "transaction value" has to include the cost which the buyer incurs, or makes provision for, or on behalf of the assessee, for advertising or publicity charges. Court judgements delivered on this issue under the earlier Section 4, or the Rules made thereunder, will not apply w.e.f. 1.7.2000, in view of the definition of "transaction value" However, where the brand name/copyright owner gets his goods manufactured from outside (on job-work or otherwise), the expenditure incurred by the brand name/copyright owner on advertisement and publicity charges, in respect of the said goods, will not be added to the assessable value, as such expenditure is not incurred on behalf of the manufacturer (assessee). [Also refer Board's Circular 619/10/2002 CX dt 19.2.2002]]
7.	What about the cost of after sales service charges and pre delivery inspection (PDI) charges, incurred by the dealer during the warranty period ?	Since these services are provided free by the dealer on behalf of the assessee, the cost towards this is included in the dealer's margin (or reimbursed to him). This is one of the considerations for sale of the goods (motor vehicles, consumer items etc.) to the dealer and will therefore be governed by Rule 6 of the Valuation Rules on the same grounds as indicated in respect of Advertisement and Publicity charges. That is, in such cases the after sales service charges and PDI charges will be included in the assessable value.
8.	Will delayed payment charges be excluded from the transaction value?	Yes, since " transaction value" relates to the price paid or payable for the goods. In this case the delayed payment charge is nothing but the interest on the price of the goods which is not paid during the normal credit period. However, to be admissible as deduction it should be separately shown or indicated in the invoice and should be charged over and above the sale price of the goods. Attention in this regard is invited to Board's Circular No. 194/28/96–CX dated 29.3.1996 which is still relevant so far as this element is concerned. [Also refer to para 8 of Board's letter F.No.354/81/2000-TRU dt 30.6.2000]
9.	Is cash discount an admissible deduction?	Since valuation is now based on "transaction value" the cash discount, if actually passed on to the buyers, will be allowed as deduction, the transaction being on principal to principal basis.
10.	Should erection, installation and commissioning charges be included in the	If the final product is not excisable, the question of including these charges in the assessable

	assessable value	value of the product does not arise. As for example, since a Steel Plant, as a whole, is an immovable property and therefore not excisable, no duty would be payable on the cost of erection, installation and commissioning of the steel plant. Similarly, if a machine is cleared from a factory on payment of appropriate duty and later on taken to the premises of the buyer for installation/erection and commissioning into an immovable property, no further duty would be payable. On the other hand if parts/components of a generator are brought to a site and the generator erected/installed and commissioned at the site then, the generator being an excisable commodity, the cost of erection, installation and commissioning charges would be included in its assessable value. In other words if the expenditure on erection, installation and commissioning has been incurred to bring into existence any excisable goods, these charges would be included in the assessable value of the goods. If these costs are incurred to bring into existence some immovable property, they will not be included in the assessable value of such resultant property.[Refer Board's 37B Order No 58/1/2002 – CX dt 15.1.2002]
11	How will valuation be done in cases of job-work?	Please also refer to Board's Circular No.619/10/2002 – CX dt 19.2.2002. Cost of transporting the raw materials/inputs to the premises of the job-worker will also be added to determine the cost of the raw material/input.[1997(071)ECR381(TRIB)]
12	How will valuation be done when goods are sold partly to related persons and partly to independent buyers?	There is no specific rule covering such a contingency. Transaction value in respect of sales to unrelated buyers cannot be adopted for sales to related buyers since as per section 4(1) transaction value is to be determined for each removal. For sales to unrelated buyers valuation will be done as per section 4(1)(a) and for sale of the same goods to related buyers recourse will have to be taken to the residuary rule 11 read with rule 9 (or 10). Rule 9 cannot be applied in such cases directly since it covers only those cases where all the sales are to be related to buyers only.
13	How will valuation of samples be done which are distributed free, as part of marketing strategy, or as gifts or donations?	Since the goods are not sold section 4(1)(a) will not apply and recourse will have to be taken to the Valuation Rules. No specific rule covers such a contingency. Except rule 8 all the other rules cover contingencies where sale is involved in some form or the other. Therefore, the residuary rule 11 will have to be adopted along with the spirit of rule 8. In other words, the assessable

		value would be 115% of the 'cost of production or manufacture' of the goods.
14	How will valuation be done when inputs or capital goods, on which CENVAT credit has been taken, are removed as such from the factory, under the erstwhile sub rule (1C) of rule 57AB of the Central Excise Rules, 1944, or under rule 3(4) of the Cenvat Credit Rules, 2001 or 2002?	Where inputs or capital goods, on which credit has been taken, are removed as such on sale, there should be no problem in ascertaining the transaction value by application of sec.4(1)(a) or the Valuation Rules. [provided tariff values have not been fixed for the inputs or they are not assessed under Section 4A on the basis of MRP] There may be cases where the inputs or capital goods are removed as such to a sister unit of the assessee or to another factory of the same company and where no sale is involved. It may be noticed that sub rule (1C) of Rule 57AB of the erstwhile Central Excise Rules, 1944 and Rule3(4) of the Cenvat Credit Rules, 2001(now 2002), talk of determination of value for "such goods" and not the "said goods". Thus, if the assessee partly sells the inputs to independent buyers and partly transfers to its sister units, the transaction value of "such goods" would be available in the form of the transaction value of inputs sold to an unrelated buyer (if the sale price to the unrelated buyer varies over a period of time, the value nearest to the time of removal should be adopted). Problems will, however, arise where the assessee does not sell the inputs/capital goods to any independent buyer and the only removal of such input/capital goods, outside the factory, is in the nature of transfer to a sister unit. In such a case proviso to rule 9 will apply and provisions of rule 8 of the valuation rules would have to be invoked. However, this would require determination of the 'cost of production or manufacture', which would not be possible since the said inputs/capital goods have been received by the assessee from outside and have not been produced or manufactured in his factory. Recourse will, therefore, have to be taken to the residuary rule 11 of the valuation rules and the value determined using reasonable means consistent with the principles and general provisions of the valuation rules and sub-section (1) of sec.4 of the Act. In that case it would be reasonable to adopt the value shown in the invoice on the basis of which CENVAT credit was taken by the assessee in the first place. In respect of capital goods adequate depreciation may be given as per the rates fixed in letter F.No.495/16/93 –Cus VI dated 26.5.93, issued on the Customs side.

ANNEXURE-C

Circular No. 692/08/2003-CX

13th February, 2003

F.No.6/29/2002-CX.I

Government of India

Ministry of Finance and Company Affairs

Department of Revenue

Subject :- Valuation of goods captively consumed.

I am directed to say that on introduction of Central Excise Valuation (Determination of Price of Excisable goods) Rules, 2000, w.e.f. 1.7.2000, it was clarified by the Board vide Circular No.354/81/2000-TRU dated 30.6.2000 (para 21) that for valuing goods which are captively consumed, the general principles of costing would be adopted for applying Rule 8. The Board has interacted with the Institute of Cost & Works Accountants of India (ICWAI) for developing costing standards for costing of captively consumed goods.

- (2) The Institute of Cost & Works Accountants of India [ICWAI] has since developed the Cost Accounting Standards, CAS 2, 3 and 4, on capacity determination, overheads & cost of production for captive consumption, respectively, which were released by the Chairman, CBEC on 23.1.2003.
- (3) It is, therefore, clarified that cost of production of captively consumed goods will henceforth be done strictly in accordance with CAS-4. Copies of CAS-4 may be obtained from the local Chapter of ICWAI.
- (4) Board's Circular No.258/92/96-CX dated 30.10.96, may be deemed to be modified accordingly so far as it relates to determination of cost of production for captively consumed goods.
- (5) This Circular may be brought to the notice of the field formations.
- (6) Suitable Trade Notices may be issued for the benefit of the Trade.
- (7) Hindi version will follow.
- (8) Receipt of these instructions may be acknowledged.

ANNEXURE-D

CASE NO.:

Appeal (civil) 2947-2948 of 2001

PETITIONER:

Commissioner of Central Excise, Pune

RESPONDENT:

M/s. Cadbury India Ltd.

DATE OF JUDGMENT: 01/08/2006

BENCH:

Ashok Bhan & Markandey Katju

JUDGMENT:

(with Civil Appeal Nos.1856-1857/2002, 5232-5233/2003,1425/2005 and 2878-2879/2005)

MARKANDEY KATJU, J.

Civil Appeals Nos. 2947-2948/2001 have been filed against the impugned final order dated 28.9.2000 passed by the Customs Excise and Gold (Control) Appellate Tribunal, West Regional Bench at Mumbai in Appeal No.E/1021, 1022/2000-MUN.

Heard learned counsel for the parties.

The question involved in these appeals is about the valuation of milk crumbs, refined milk chocolate and four other products manufactured by the respondent - M/s. Cadbury India Limited, in its factory at Induri, Pune and captively consumed in that factory and other factories of the respondent in the manufacture of chocolate. No part of these products are sold by the respondent.

The respondent had sought valuation of these goods under Rule 6(b)(ii) of the Central Excise (Valuation) Rules, which provides for basing the valuation on such goods on the "cost of production on manufacture including profits, if any, the assessee would have earned in the sale of such goods."

The assessee had showed the price of these goods supported by a statement verified by a chartered accountant. The statement indicated the cost of edible and packing material used in the manufacture including its overheads. A separate statement in support of the profit added was formulated and these assessments were provisionally approved.

At the time of the finalization of the assessment, the department took the view that the value of the goods should include the labour cost, direct expenses, total factory expense, administration expenses, travelling expense, insurance premium, advertising expense and interest. The Assistant Commissioner added these elements to the declared value. He added the total expenses of the company as shown in the balance sheet and deducted the cost material. A percentage of this cost of the remaining figure was treated as the factor by which the assessable value should be increased.

In appeal the Commissioner (Appeals) upheld the order of the Assistant Commissioner. He held that since Rule 6(b)(ii) itself specified including the profit on the goods captively consumed hence this indicated the intention in the rule that the valuation should be brought to the level of the sale value of the goods and hence this includes all expenses referred to above. The Commissioner (Appeals) also relied on the circular dated 30.10.1996 issued by the Board relating to captively consumed goods. He has also relied upon paragraph 49 of the Supreme Court's judgment in Union of India vs. Bombay Tyres International AIR 1984 SC 420.

In further appeal the Tribunal set aside the orders of the Commissioner and the Assistant Commissioner. The Tribunal held that sub-rule (ii) of Rule 6(b) can be invoked only in a situation where the goods are not sold and there are no comparable goods. The Tribunal held that the expenses other than the cost of manufacture, cost of raw materials and the profit would not be includible in the assessable value.

The issue in the present case is about the value of the goods captively consumed by the respondent. The assessee has contended that there is no dispute that these intermediate goods are not marketable and are not bought and sold in the market. Hence the valuation of these intermediate goods has to be done according to Rule 6(b)(ii) of the Central Excise (Valuation) Rules, 1975.

Rule 6(b)(ii) reads as follows:

"Rule 6 If the value of the excisable goods under assessment cannot be determined under Rule 4 or Rule 5, and

(a)

(b)(i)

(ii) if the value cannot be determined under sub-clause (i), on the cost of production or

manufacture including profits, if any, which the assessee would have normally earned on the sale of such goods; "

According to settled principles of accountancy only the elements that have actually gone into the manufacture/production of these intermediates i.e. sum total of the direct labor cost, direct material cost, direct cost of manufacture and the factory overheads of the factory producing such intermediate products are included in the cost of production. The Appellant produced alongwith the reply to the Show Cause Notice the following authoritative texts: Wheldon's Cost Accounting and Costing Methods, Cost Accounting methods by B K Bhar, Principles of Cost Accounting by N.K. Prasad, Glossary of Management Accounting Terms by ICWAI.

In CCE v. Dai Ichi Karkaria Ltd., (1999) 7 SCC 448, at page 459 it has been held that the normal principles of accountancy shall be applied to determine the cost. In this decision this Court observed :

"Learned Counsel for the respondents drew our attention to the judgment of this Court in Challapalli Sugar Ltd. v. CIT. The Court was concerned with "written-down value". The "written-down value" had to be taken into consideration while considering the question of deduction on account of depreciation and development rebate under the Income Tax Act. "Written-down value" depended upon the "actual cost" of the assets to the assessee.

The expression "actual cost" had not been defined in the Income Tax Act, 1922 and the question was whether the interest paid before the commencement of production on the amount borrowed for the acquisition and installation of the plant and machinery could be considered to be a part of the "actual cost" of the assets to the assessee. As the expression "actual cost" had not been defined, this Court was of the view that it should be construed "in the sense which no commercial man would misunderstand. For this purpose, it could be necessary to ascertain the connotation of the above expression in accordance with the normal rules of accountancy prevailing in commerce and industry". Having considered authoritative books in this regard, this Court said that the accepted accountancy rule for determining the cost of fixed assets was to include all expenditure necessary to bring such assets into existence and to put them in a working condition. That rule of accountancy had to be adopted for determining the "actual cost" of the assets in the absence of any statutory definition or other indication to the contrary."

Subsequent to the filing of these appeals, the Institute of Cost and Works Accountants of India (ICWAI) has laid down the principles of determining cost of production for captive consumption and formulated the standards for costing : CAS-4. According to CAS-4 the definition of "cost of production" is as under :

"4.1. Cost of Production : Cost of Production shall consist of Material consumed, Direct wages and salaries, Direct expenses, Works overheads, Quality Control cost, Research and Development cost, Packing cost, Administrative Overheads relating to production."

The cost accounting principles laid down by ICWAI have been recognized by the Central Board of Excise and Customs vide Circular No.692/8/2003 CX dated 13.2.2003. The circular requires the department to determine the cost of production of captively consumed goods strictly in accordance with CAS-4.

The Tribunal in the case of BMF BELTINGS LTD. vs. CCE : 2005 (184) E.L.T. 158 (Tri. Bang.) for the period 1995 to 2000 has directed the department to apply CAS-4 for the determination of the cost of production of the captively consumed goods. In ITC vs. CCE (190) ELT 119 the Tribunal held that the department has to calculate the cost of production in terms of CAS-4. Other decisions of the

Tribunal, wherein it has directed that CAS-4 be applied for determination of the cost of production, are Teja Engineering v/s CCE 2006 (193) ELT 100 (Tri-Chennai), Ashima Denims v/s CCE 2005 (191) ELT 318 (Tri- Mumbai), and Arti Industries vs. CCE 2005 (186) ELT 208 (Tri-Chennai). This is therefore a consistent view taken by the Tribunal. The department has not filed any appeal in these cases and accepted the legal position.

Apart from this, in the light of several decisions of this Court, the Department is also bound by the said circular No.692/8/2003 CX dated 13.2.2003 issued by the CBEC.

As such it cannot now take a contrary stand.

It may be noted that in the present case the intermediate products (milk crumbs, refined milk chocolate and four other intermediate products) are captively consumed in the Respondent's own factory. These intermediate products are not sold nor are marketable.

Hence there can be no question of including the expenses of the factory which produces the final product namely the chocolate e.g. advertising, insurance and another expenses in their valuation as was sought to be added by the Commissioner (Appeals) and the Assistant Commissioner.

For the reasons given above, we find no merit in these appeals and they are dismissed. No costs.

Civil Appeal Nos. 1856-1957/2002, 5232-5233/2003, 1425/2005 & 2878-2879/2005)

In view of the decision in Civil Appeal Nos. 2947-2948/2001, these appeals are accordingly dismissed. No costs.

ANNEXURE -E

EXCISE LAW TIMES

Date – 16 March 2009

Volume No. 235 Part 3

DEPARTMENTAL CLARIFICATION

Minutes of RAC/PGC Meetings

Regional Advisory Committee – Minutes of RAC Meeting of Pune Commissionerate (Extracts)

The RAC meeting for the quarter ending December 2008 and PGC meeting for the month of January 2009 was held on 3 February at 15.00hrs. at Excise Bhawan Akurdi, Dr. Ambedkar Road, Near Akurdi Railways Station, Akurdi, Pune –I Central Excise Commissionerate. The meeting was chaired by Smt. Vasudev Commissioner, Central Excise Pune – I Commissionerate.

The following PGC / RAC members and departmental officers attended the meeting.

Point received from J. L. Jakhotia, Member PGC / RAC

The finished goods is being sold for home consumption and is also stock transferred to the assessee's another unit. As per settled law, if the factory gate price is available, the valuation Rule 8 is not applicable but the clearance to another unit has to be effected under Section 4 of C.E. Act. The assessee has paid the duty under section 4 for stock transferred goods, however, the Range Superintendent is insisting for CAS-4 Certification which in no way required under the law.

The matter requires clarification.

It is not specified if the goods are transferred to assessee's another unit for further consumption or it is to be sold from there. If the goods are stock transferred for further consumption to assessee's another unit then valuation is to be done as per Section 4(1) (b) which says. - ---

4(1) (b) in any other case, including the case where the goods are not sold be the value determined in such manner as may be prescribed. This valuation has to be done as prescribed under Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000.

The Valuation for such transactions will be done under Rule 9 read with Rule 8 of the Valuation Rules, 2000 which says – where the excisable goods are not sold by the assessee but are used for

consumption by him or on his behalf in the production or manufacture of other articles, the value shall be [one hundred and ten percent] of the cost of production or manufacture of such goods.

Therefore, the Range Superintendent insistence for CAS-4 appears to be correct.

ANNEXURE-F

[TO BE PUBLISHED IN THE GAZETTE OF INDIA, EXTRAORDINARY, PART II,
SECTION 3, SUB SECTION (i)]

GOVERNMENT OF INDIA
MINISTRY OF FINANCE
DEPARTMENT OF REVENUE

Notification No 14/2013 – Central Excise (N.T.)

New Delhi, the 22nd November, 2013
01, Agrahayan 1935 Saka

G.S.R. (E). - In exercise of the powers conferred by section 37 of the Central Excise Act, 1944 (1 of 1944), the Central Government hereby makes the following rules to further amend the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, namely:-

1. (1) These rules may be called the Central Excise Valuation (Determination of Price of Excisable Goods) Amendment Rules, 2013.
(2) They shall come into force with effect from the 1st day of December, 2013.

2. In the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 (hereinafter referred to as the said rules), for rule 8, the following rule shall be substituted, namely:-

“8. Where whole or part of the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value of such goods that are consumed shall be one hundred and ten per cent of the cost of production or manufacture of such goods.”

3. In the said rules, in rule 9, for the words “When the assessee so arranges that the excisable goods are not sold by an assessee except to or through a person who is related in the manner specified in any of the sub-clauses (ii), (iii) or (iv) of clause (b) of sub-section (3) of section 4 of the Act, the value of the goods shall be the normal transaction value”, the words “Where whole or part of the excisable goods are sold by the assessee to or through a person who is related in the manner specified in any of the sub-clauses (ii), (iii) or (iv) of clause (b) of sub-section (3) of section 4 of the Act, the value of such goods shall be the normal transaction value” shall be substituted.

4. In the said rules, in rule 10, for the words “When the assessee so arranges that the excisable goods are not sold by him except to or through an inter-connected undertaking, the value of goods shall be determined in the following manner, namely:- ” the words “Where whole or part of the excisable goods are sold by the assessee to or through an inter-connected undertaking, the value of such goods shall be determined in the following manner, namely:- ” shall be substituted.

F. No. 6/12/2009-CX-1

(For Private Circulation Only)

(Pankaj Jain)
Under Secretary to the Government of India

Note - The principal rules were published in the Gazette of India, Extraordinary, Part II, Section 3, sub-section (i) vide notification No. 45/2000-Central Excise (N.T.), G.S.R. 575(E), dated the 30th June, 2000 and was last amended vide notification No. 9/2007 – C.E. (N.T.), G.S.R 149 (E), dated the 1st March, 2007.