

Chapter 4 : Cenvat Credit

A manufacturer/service provider utilises capital goods such as plant and machinery, inputs such as raw material and input services such as security services, management, maintenance or repair services, etc. in the manufacture of a final product. The Central Excise Duty/Service Tax paid on any of these three items is credited into a Cenvat credit account. Accumulated credit may be used for making duty/tax on finished goods/output services subject to fulfilment of certain conditions. This ensures that the inputs are taxed only once.

During the course of this audit, we found 144 cases of incorrect availing of Cenvat credit with duty impact of ` 6.74 crore. The Ministry/department agreed with our observations in 72 of these cases, involving duty of ` 3.50 crore and recovered ` 3.33 crore in 70 cases. We have illustrated a few of these cases in the following paragraphs.

4.1 Irregular availing of Cenvat credit

Rule 3(1) of the Cenvat Credit Rules, 2004, specifies the duties of excise and Service Tax, which can be availed as Cenvat credit by the manufacturer or service provider. There is no provision to avail credit of basic customs duty. Further, rule 14 of Cenvat Credit Rules, 2004, provides for the recovery of interest for wrong availing and utilisation of Cenvat credit.

We observed from the input Cenvat credit registers and invoices of M/s J. P. Enterprises, a manufacturer of excisable goods under Chapter 87, in Nasik Commissionerate, that the assessee availed Cenvat credit of basic customs duty on imported inputs of ` 20.17 lakh for the period during 2010-11 to 2012-13 which is inadmissible. This resulted in irregular availing of Cenvat credit of ` 20.17 lakh.

We pointed this out in March 2014.

The Ministry stated (October 2014) that an amount of ` 20.17 lakh was paid by the assessee alongwith interest of ` 6.86 lakh and penalty of ` 4.64 lakh in March 2014.

4.2 Non-reversal of Cenvat credit

As per rule 3(5B) of the Cenvat Credit Rules, 2004, where any provision is made to write off the value of inputs or capital goods, on which Cenvat credit has been taken, the manufacturer shall pay an amount equivalent to the Cenvat credit taken in respect of said input/capital goods. If the said inputs or capital goods are subsequently used in the manufacture of final products, the manufacturer shall be entitled to take credit of the amount paid earlier.

We observed that M/s Dymos Lear Automotive India Pvt. Ltd., (Unit II), in Chennai-IV Commissionerate, a manufacturer of automobile seats, availed Cenvat credit on input, capital goods and input services and utilised the same for payment of duty on their final product. The assessee created a provision to write off the value of obsolete inventories amounting to ` 1.73 crore in the accounts for the year 2012-13. The assessee deducted the said amount from the total value of inventories without reversing the Cenvat credit taken.

We pointed out the non-reversal of Cenvat credit of ` 21.40 lakh in December 2013.

The Ministry intimated (October 2014) the reversal of ` 23.50 lakh including interest by the assessee.

4.3 Availing of Cenvat credit on ineligible capital goods

The Board in its instructions dated 8 July 2010 clarified that Cenvat credit on capital goods is available only on items which are excisable goods covered under the definition of capital goods under the Cenvat Credit Rules, 2004 and used in the factory of the manufacturer. 'Capital goods' are defined in rule 2(a) of the Cenvat Credit Rules, 2004.

M/s Atharva Foundries Pvt. Ltd., in Kolhapur Commissionerate, engaged in manufacture of articles of Chapter 87, availed Cenvat credit of ` 10.94 lakh on items such as MS channel, MS Angle and HR coil during the period from 2011-12 to 2012-13 treating them as capital goods. Since these items are not covered under the definition of capital goods, the availing of Cenvat credit of ` 10.94 lakh was not admissible and was reversible.

We pointed this out in June 2013.

Accepting the audit observation, the Ministry intimated (October 2014) that a show cause notice for ` 10.94 lakh had been issued.

4.4 Short payment of Cenvat credit on clearance of used machinery

Rule 3(5A) of Cenvat Credit Rules, 2004 provides that if capital goods on which Cenvat credit has been taken, are removed after being used, the manufacturer or provider of output services shall pay an amount equal to the Cenvat credit taken on the said capital goods reduced by 2.5 per cent for each quarter of a year or part thereof from the date of taking Cenvat credit. However, if the amount so calculated is less than the amount equal to the duty leviable on transaction value, the amount to be paid shall be equal to the duty leviable on transaction value.

4.4.1 During scrutiny of records of M/s Majestic Auto Ltd., in Ludhiana Commissionerate, engaged in the manufacturing of auto parts/motor vehicle parts, we observed that the assessee transferred used machinery for ` 12.79 crore to M/s Majestic Auto Ltd., Noida during the year 2012-13, by paying excise duty of ` 113.77 lakh instead of ` 158.03 lakh leviable on transaction value. This resulted in short payment of duty of ` 44.26 lakh.

We pointed this out in March 2014.

The Ministry contested the observation stating (October 2014) that had the assessee paid the higher duty, the other unit would have availed the higher credit and that the entire exercise would have been neutral. The Ministry also cited certain Tribunal decisions in support of the payment as effected by the assessee.¹⁷

The reply is not acceptable because as per provision of 3 (5A)(a)(ii) of Cenvat Credit Rules, 2004 if the amount calculated is less than the amount equal to duty leviable on transaction value, the amount to be paid shall be equal to the duty leviable on transaction value. It is also pointed out that CBEC has not issued any instructions based on the cited Tribunal decisions to guide assessees as well as adjudicating officers in similar situations.

4.4.2 Scrutiny of records of M/s Rico Auto Industries, in Gurgaon Commissionerate, engaged in the manufacturing of parts and accessories of the motor vehicles, revealed that a fire accident had occurred in December 2012 wherein plant and machinery worth ` 4.27 crore was destroyed. We observed that Cenvat credit of ` 44.55 lakh had been availed on the same. The assessee had received insurance claim of ` one crore on the destroyed plant and machinery. However, the assessee did not pay the proportionate credit of ` 10.80 lakh after allowing the permissible deduction at 2.5 per cent

¹⁷ Ideal Components Pvt. Ltd. Vs. CCE {2009 (244) ELT 589} and Wolfra Tech. Pvt. Ltd. Vs. CCE {2012 (284) ELT 89}

of credit availed for every quarter of use from the date of installation to the date of destruction in fire.

We pointed this out in January 2014.

The Ministry intimated (October 2014) that show cause notice for `10.80 lakh is under issue.

4.5 Irregular availing of Cenvat credit of Service Tax on inadmissible input services

As per rule 2 (l) of the Cenvat Credit Rules, 2004, 'input Service' includes, *inter alia*, any service, used by a manufacturer, whether directly or indirectly, in or in relation to the manufacturer of final products and clearances of final products up to the place of removal, and includes services used in relation to setting up, modernisation, renovation or repairs of factory, premises of the provider of output service or an office relating to such factory or premises, advertisement, sales promotion, market research, storage up to the place of removal, procurement of inputs, activities relating to business such as accounting auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry and security inward transportation of input or capital goods and outward transportation up to the place of removal.

4.5.1 M/s Toyoda Gosei Minda India Pvt. Ltd. and M/s Visteon Climate Systems India Ltd., in Jaipur-I Commissionerate, engaged in the manufacture of automobile parts paid Service Tax of ` 1.46 crore during the period from 2010-11 to 2012-13 on freight outward and availed Cenvat credit of the above amount. The outward freight charges are not eligible input service. This resulted in irregular availing of Cenvat credit of ` 1.46 crore.

We pointed this out in January 2014.

The Ministry intimated (October 2014) that M/s Toyoda Gosei Minda India Pvt. Ltd. deposited the entire amount. Further, show cause notice is being issued to M/s Visteon Climate Systems India Ltd.

4.5.2 During the test check of Cenvat credit records of M/s India Yamaha Motor Pvt. Ltd., in Noida Commissionerate, we observed that the assessee availed Cenvat credit of Service Tax of ` 18.72 lakh paid on the services of rent, repair and maintenance services for its unit at Kolkata, West Bengal

during the year 2012-13. The rent, repair and maintenance services were not related to the manufacturing activity and did not relate to the assessee premises as well. This resulted in irregular availing of Cenvat credit of ` 18.72 lakh.

We pointed this out (January 2014), the reply of the Ministry/department is still awaited (October 2014).

4.5.3 Other cases of irregular availment of Cenvat credit

Besides the above cases, we observed that the assessee availed Cenvat credit irregularly in the following cases:

Table No.10

Illustrative cases of irregular availment of Cenvat credit

Name of assessee	Commissi- onerate	Period	Cenvat credit availed irregularly as observed by CERA	Reply of Ministry/department
M/s Sun Beam Auto Pvt. Ltd.	Jaipur-I	2011-12 to 2012-13	` 18.08 lakh	The Ministry intimated (October 2014) reversal of credit amounting to ` 17.91 lakh.
M/s Gestamp Automotive India Pvt. Ltd.	Pune-I	2012-13	` 5.56 lakh	The Ministry intimated (October 2014) recovery of ` 6.16 lakh including penalty.
M/s Alicon Castalloy Pvt. Ltd.	Pune-III	2011-12 to 2012-13	` 8.65 lakh	The Ministry intimated (October 2014) recovery of ` 13.07 lakh including interest and penalty.
M/s Sharda Motors Industries Ltd.	Delhi-LTU	2010-11 to 2012-13	` 37.64 lakh	The Ministry intimated (October 2014) that the assessee had made a part payment of ` 10.00 lakh.
M/s Minda Corporation Ltd.	Noida	2010-11	` 17.93 lakh	The Ministry stated (October 2014) that SCN was being issued.

4.6 Excess availing of input service credit

As per rule 2(l) of the Cenvat Credit Rules, 2004, 'input service' means any service used by the manufacturer in or in relation to the manufacture of final products and clearance thereof up to the place of removal. Under reverse charge mechanism, person receiving certain services which, *inter alia*, includes sponsorship service, is liable to pay tax as per provisions contained in rule 2(1)(d) of Service Tax Rules, 1994.

4.6.1 Examination of records of M/s Force Motors Ltd. in Pune I Commissionerate revealed that the assessee had received sponsorship

services from various entities for which the payments were made by the assessee. The unit located at Akurdi has discharged the Service Tax liability and availed input service credit. We observed that the assessee has more than one unit at different locations in the country, manufacturing various vehicles such as traveller, tempos, tractors etc. Since the sponsorship services were incurred for the company as a whole and were used directly or indirectly for the entire company, the availing of Cenvat credit alone by Akurdi unit was not proper. The assessee had availed the input service credit of ` 13.12 lakh on sponsorship service during the year 2012-13. The input service credit attributable to Akurdi unit works out to only ` 1.89 lakh. This resulted in excess availing of Cenvat credit of ` 11.23 lakh.

We pointed this out in February 2014.

Accepting the observation, the Ministry intimated (October 2014) that show cause notice had been issued for ` 12.30 lakh.

4.6.2 Notification dated 16 December 2002, exempts the taxable services provided by a consulting engineer to a client on transfer of technology from so much of the Service Tax leviable thereon under Section 66 of the Finance Act, 1994, as is equivalent to the amount of cess paid on the said transfer of technology under the Section 3 of the Research and Development Cess Act, 1986.

During test check of records of M/s Mitsubishi Electric Automotive India Pvt. Ltd. in Gurgaon Commissionerate, Audit observed that the assessee had paid Service Tax of ` 61.20 lakh on royalty and technical fee on a value of ` 5.93 crore during the period 2010-11 to 2011-12 and availed Cenvat credit of the full amount. We observed that out of ` 61.20 lakh, an amount of ` 28.40 lakh was deposited against R and D cess by the assessee. Hence, availing of full credit without deducting the R and D cess amount as per notification dated 16 December 2002 resulted in excess availing of Cenvat credit of ` 28.40 lakh.

We pointed this out in February 2014.

The Ministry intimated (October 2014) that a show cause notice is under process for issue.

4.7 Availing of Cenvat credit relating to commission paid to sales agents

As per rule 2(l) of the Cenvat Credit Rules, 2004, sales promotion is included in the definition of input service. The Hon'ble High Court of Gujarat held in M/s Cadila Healthcare Ltd. that Cenvat credit of Service Tax paid on the commission to the commission agents causing sale of goods, is ineligible for input service credit¹⁸. Commission Agent is a person who is directly concerned with the sale or purchase of goods and is not connected with the sales promotion. Hence, activity of sales commission does not fall under the category of sales promotion in "input service" definition.

We observed the following instances where Cenvat credit was availed in respect of Service Tax paid to commission agents/ on sales commission. We pointed out that this was to be reversed alongwith interest.

Table No.11

Illustrative cases relating to commission paid to sales agents

Name of assessee	Commissi- onerate	Period	Cenvat credit availed irregularly as observed by CERA	Reply of Ministry/department
M/s Maini Materials Movement Pvt. Ltd.	Bengaluru -I	2011-12 to 2012-13	` 5.33 lakh	Ministry intimated (October 2014) that show cause notice is under issue.
M/s Remsons Industries Ltd.	Daman	2010-11 to 2012-13	` 10.76 lakh	Ministry intimated (October 2014) that show cause notice is under issue.
M/s Sealtite Dichtungs Pvt. Ltd.	Bengaluru -I	2012-13	` 2.55 lakh	Ministry intimated (October 2014) that the assessee reversed the irregular Cenvat credit of ` 3.41 lakh alongwith interest under protest.
M/s Honda cars (India) Ltd.	Delhi-LTU	2010-11 to 2012-13	` 4.72 lakh	Department replied (May 2014) that credit of ST on sales commission is admissible in view of the definition of 'business auxiliary services' and 'commission agent' given in the Finance Act, and specific clarification given by Tax Research Unit (TRU) on the subject.

¹⁸{2013 (30) STR 3 (Gujarat)}

				Audit remarks: The reply is not acceptable in view of the judgement of the Gujarat High Court.
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4.8 Incorrect availing of Cenvat credit on exempted services

As per rule 6 of Cenvat Credit Rules, 2004, where a manufacturer manufactures dutiable as well as exempted goods, separate accounts shall be maintained for the receipt and use of input services used for the provision of exempted services. Alternatively, the manufacturer or service provider shall pay an amount as per rule 6(3) of Cenvat Credit Rules, 2004. Rule 2(e) of Cenvat Credit Rules as amended with effect from 1 April 2011 states that 'exempted service' also includes trading. Further, as per Explanation I(c) to rule 6(3A), in case of trading, value of 'exempted service' shall be the difference between the sale price and the purchase price of the goods traded or ten per cent of the cost of goods sold, whichever is more.

4.8.1 During test check of records of M/s Savita Auto Industries in Nagpur Commissionerate, we observed that the assessee carried out, *inter alia*, trading activity. The assessee also availed Cenvat credit on common input services such as security, transportation, computer maintenance etc. used both for manufacturing of excisable goods as well as trading of goods. This amounted to `59.72 lakh during the period 2010-11 to 2012-13. The assessee had not maintained separate accounts as required under the Rules. Since trading is an exempted service, the assessee was not eligible to avail Cenvat credit of the input services used for providing the exempted services and was liable to pay duty.

We pointed this out in December 2013.

The Ministry admitted (October 2014) the observation.

We await further progress (October 2014).

4.8.2 Similarly, M/s India Yamaha Motors (P) Ltd., in Noida Commissionerate was engaged in the manufacturing of two-wheelers as well as in their trading. During 2011-12 and 2012-13, the assessee availed common input services for manufacturing and trading activities but did not maintain separate account. Since trading is an exempted service, the assessee was not eligible to avail Cenvat credit of the input services used for providing the exempted services and was liable to pay duty.

In the absence of adequate data for quantification, Audit could not quantify the non-payment of duty.

We pointed this out in December 2013. We await the Ministry's response (October 2014).

4.9 Irregular utilisation of Cenvat credit

As per rule 3(4) of the Cenvat Credit Rules, 2004, Cenvat credit shall be utilised only to the extent such credit is available on the last day of the month or quarter, as the case may be, for payment of duty or tax relating to that period. Board's circular dated 28 March 2012 clarifies that the above rule provision is applicable for the normal payment of duty after due date.

4.9.1 During test check of records of M/s M&M Machine Craft Ltd. in Gurgaon Commissionerate, we observed that the assessee paid Central Excise duty of ` 37.42 lakh on account of issuance of supplementary invoices for the period 2010-11 to 2012-13 by utilising Cenvat credit earned subsequent to the respective periods. The Cenvat credit available for the respective months had already been utilised at the time of payment of Central Excise duty at the time of issuing original invoices. This resulted in irregular utilisation of Cenvat credit of ` 37.42 lakh.

We pointed this out in January 2014.

The Ministry intimated (October 2014) that show cause notice for ` 42.42 lakh has been issued to the assessee.

4.9.2 M/s Natesan Synchrocones Pvt. Ltd. in Chennai IV Commissionerate availed an excess Cenvat credit of ` 7.58 lakh due to double credit on 31 July 2012 and utilised an amount of ` 6.77 lakh towards payment of duty for the month of July 2012. The Internal Audit wing has pointed out this mistake and assessee has reversed an amount of ` 7.58 lakh in the Cenvat account on 15 March 2013 and paid ` 0.12 lakh towards interest.

Since the excess Cenvat credit of ` 6.77 lakh was already utilised by the assessee for duty payment, the amount of ` 6.77 lakh should be payable by cash and not to be reversed in the Cenvat account. This resulted in irregular utilisation of ` 6.77 lakh.

We pointed this out in December 2013.

The Ministry contested the observation stating (October 2014) that the assessee reversed the excess credit when the mistake was pointed out in internal audit and there is no default in payment of excise duty as per rule

8(3A) of Central Excise Rules, 2002.

The reply of the Ministry is not tenable since our audit observation was that had the assessee not taken credit twice, there would not have been enough credit at the end of July 2012 to adjust the duty of ` 6.77 lakh.