

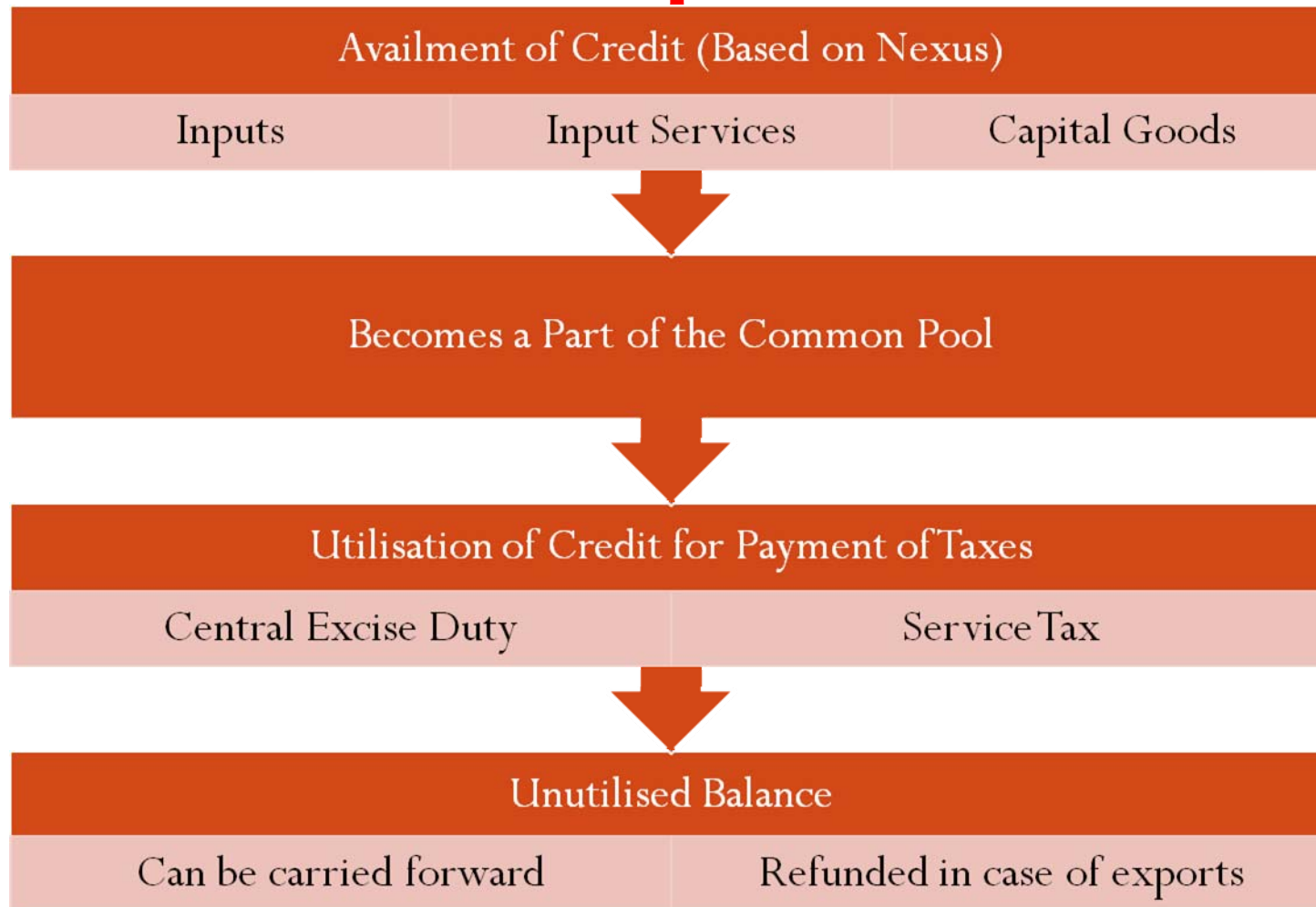
# Controversies in CENVAT Credit

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# Basic Points

- CENVAT Credit intended to grant relief from cascading effect of central level indirect taxes (central excise duty, service tax and cess thereon)
- Governed by CENVAT Credit Rules, 2004 as amended from time to time
- Works on Passbook Concept

# Passbook Concept



## Some Definitions:

- “final products” means excisable goods manufactured and produced from input or using input service – Rule 2(h)
- “exempted goods” means excisable goods which are exempt from the whole of the duty of excise leviable thereon and includes goods which are chargeable to “Nil” rate of duty – Rule 2(d)
- “output service” means any taxable service excluding the taxable service referred to in sub clause (zzp) of clause (105) of section 65 of the Finance Act provided by the provider of taxable service to a customer, client, subscriber, policy holder or any other person as the case may be and the expression ‘provider’ and ‘provided’ shall be construed accordingly – Rule 2(p)
- “exempted services” means taxable services which are exempt from the whole of the service tax leviable thereon and includes services on which no service tax is leviable under section 66 of the Finance Act – Rule 2(e)

# Nexus for Availment

Nexus with Output	Inputs	Input Services	Capital Goods
Final Products Output Service	Available Rule 3	Available Rule 3	Available Rule 3
Exempted Goods	Not Available Rule 6(1)	Not Available Rule 6(1)	Not Available Rule 6(4)
Exempted Service	Not Available Rule 6(1) r.w. R. 2(a)	Not Available Rule 6(1) r.w. Rule 2(a)	Not Available Rule 6(4) r.w. R. 2(a)
Taxable as well as Exempted Goods/Services	Available subject to the provisions of Rules 6(2) & 6(3)	Available subject to the provisions of Rules 6(2), 6(3) & 6(5)	Available Rule 3
Other Combinations	No Rules Framed	No Rules Framed	No Rules Framed

## Issues on Nexus:

- Services governed by Rule 2(1)(d) of Service Tax Rules
  - whether to be treated as taxable services in the case of service provider?
- Export of Services governed by Rule 4 of Export of Services Rules
  - Question 6 of Circular 868/6/2008-CX dated 09-05-2008
- Services to units located in SEZ
  - Not an export as per Export of Services Rules
  - Exempted from whole of service tax – Notification 4/2004-ST

# Issues on Nexus:

- Services rendered outside the territorial jurisdiction - J&K / NDA/ Outside India
  - Is there a difference between these services and export of services?
  - Are these either output services or exempted services?
- Trading in Goods
  - Are these final products (or exempted goods)?
  - Are these either output services or exempted services?
- Investment Incomes / Surplus
  - Are these either output services or exempted services?
- Prohibitions under other Notifications
  - Notification 1/2006-ST dated 01-03-2006 read with Explanation to Rule 3

# “Input Services”

"input service" means any service,—

- (i) used by a provider of taxable service for providing an output service; or
- (ii) used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products upto the place of removal,

and includes services used in relation to setting up, modernization, renovation or repairs of a factory, premises of provider of output service or an office relating to such factory or premises, advertisement or sales promotion, market research, storage upto the place of removal, procurement of inputs, 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 inputs or capital goods and outward transportation upto the place of removal;



# Input Services

- Basic Limb
  - Requires the “use” of the service for provision of “output service”
  - In case of manufacturers, only services upto the place of removal eligible
- Whether “use” can include “intended for use”?
  - BPL Display Devices Limited vs. Commissioner of Central Excise 2004 (174) E.L.T. 5 (S.C.)
  - Commissioner of Customs vs. Suraj Industries Limited 2006 (198) E.L.T. 199 (Tri. - Del.)
- Inclusive Limb – How wide is it? Especially the phrase “activities relating to business”?

# Some Illustrations..

Illustration	Whether Available	Comments
Mobile Phones	Yes	Circular issued under Service Tax Credit Rules no longer valid
Residential Telephone Bills of Directors/Employees/Partners/Proprietors	Debatable	Against: HEG Ltd. 223 ELT 212 International Testing Centre 10 STR 253 Favourable:
Employee Welfare Activities like health insurance, garden maintenance, construction of residential colonies, etc.	Debatable	Against: HEG Ltd. 223 ELT 212 VMT Spinning Co. 2008 TIOL 5 ARA Favourable: Manikgarh Cement 9 STR 554 Century Cement 2008 TIOL 1706
Canteen Services	Yes	GTC Industries 2008 TIOL 1634 (Mum LB)

# Inputs

- All Goods used in relation to manufacture of final products within the factory of production
- All Goods used for providing any output service
- Does not include LDO/HSD/Motor Spirit
- Includes inputs used in manufacture of capital goods which are used in the factory for manufacture
  
- Whether credit can be claimed on cement and steel (Refer Mundra Port & Special Economic Zone Ltd.)
  - By the service provider who has bought the same for captive consumption?
  - By the contractor?

# Capital Goods

- Goods falling in Excise Tariffs:
  - Chapter 82 (Tools & Implements of Base Metals)
  - Chapter 84 (Machinery & Mechanical Equipments)
  - Chapter 85 (Electrical Machinery & Equipments)
  - Chapter 90 (Technical Instruments)
  - Headings 68.04 & 68.05
- Spares, Components & Accessories
- Pollution Control Equipment, Refractories & Refractory Material, Moulds & Dies, jigs & fixtures, Tubes & Pipes, Storage Tanks
- Motor Vehicles for specified service providers
- Credit Available subject to non claim of Depreciation

## Utilisation : Rules 3(4) & 3(7)(b)

Availment	Excise Duty	Service Tax	Educ. Cess	SHE
Excise Duty / CVD / Service Tax	✓	✓	✓	✓
ADC	✓	✗	✓ / ✗	✓ / ✗
Education Cess	✗	✗	✓	✗
SHE	✗	✗	✗	✓

# Utilisation of Credit: Reverse Charge Cases

- CENVAT Credit can be utilised for payment of tax on output service – Rule 3(4)(e)
- Output Service defined under Rule 2(p) – An Explanation deeming input service to be output service dropped with effect from 19-04-06. Prior to that, various decisions permitted the utilisation of credit.
- In general, with the omission of Explanation, no credit can be utilised for payment of tax under reverse charge (like goods transport services, sponsorship services, etc.)
- However, the tax once paid can be availed as credit if otherwise eligible

# Utilisation of Credit: Import of Services

- Section 66A of Finance Act deems an “import of service” to have been provided by the recipient – accordingly, an import of service becomes an output service?
- Rule 5 of Taxation of Services (Provided from Outside India and Received in India) Rules:
  - The taxable services provided from outside India and received in India shall not be treated as output services for the purpose of availing credit of duty of excise paid on any input or service tax paid on any input services under CENVAT Credit Rules, 2004
- Whether the Rule restricts availment or utilisation?
- What is the intention of listing excise paid on any input?
- Why is capital goods missed out?
- Can accumulated credit be utilised for payment of service tax on import of services?

# CENVAT & Non Taxable Activities

- Rule 6(1): Not Available for Exempted Goods or Services
- Rule 6(2): Specific Identification and claim for taxable goods / services – OPTION I
- Rule 6(3)(i): No identification – composite scheme for manufacturers / service providers based on output (ad hoc payment) – OPTION II
- Rule 6(3)(ii): No identification – composite scheme for manufacturers / service providers based on input (proportionate payment) – OPTION III



# CENVAT: Option I

- Maintain Separate Records and claim FULL credit of inputs and input services attributable to taxable output services / taxable finished goods – Rule 6(2)
- Claim FULL Credit of Capital Goods unless exclusively used for exempted services/ exempted finished goods – Rule 6(4)
- Claim FULL Credit of Specified Input Services unless exclusively used for exempted services/ exempted finished goods – Rule 6(5)

# CENVAT: Option II

- Claim FULL Credit of Inputs unless exclusively used for exempted services/ exempted finished goods
  - Claim FULL Credit of Input Services unless exclusively used for exempted services/ exempted finished goods
  - Claim FULL Credit of Capital Goods unless exclusively used for exempted services/ exempted finished goods – Rule 6(4)
  - Claim FULL Credit of Specified Input Services unless exclusively used for exempted services/ exempted finished goods – Rule 6(5)
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- Pay an Amount equal to 10% of value of exempted goods (EG) Rule 6(3)(i)
  - Pay an Amount equal to 8% of value of exempted services (ES) Rule 6(3)(i)

# CENVAT: Option III

- Effectively Claim PROPORTIONATE Credit of Inputs unless exclusively used for exempted services/ exempted finished goods
  - Manufacturer Input Quantity Based
  - Service Provider Output Value Based
- Effectively Claim PROPORTIONATE Credit of Input Services unless exclusively used for exempted services ES/ exempted finished goods EG– Rule 6(3)(i)
- Claim FULL Credit of Capital Goods unless exclusively used for exempted services/ exempted finished goods – Rule 6(4)
- Claim FULL Credit of Specified Input Services unless exclusively used for exempted services/ exempted finished goods – Rule 6(5)
- Denominator (D) includes ES + EG + TS + TG
- PROPORTIONATE CREDIT to be worked on Provisional and Final Basis

## CENVAT Option III (Contd.)

- Provisional Percentage to be based on previous financial year (can be Zero)
- Final Percentage to be based on current financial year
- Pay Difference before 30 June (otherwise pay interest@ 24% p.a.)
- Excess can be re-claimed as “Credit” – need not be subject to fresh proportion
- Intimate details to Superintendent within 15 days

# CENVAT & Composite Output

- Exercise Option II/III across all activities
  - Circular 868/6/2008-CX dated 09-05-2008 Q. 2
- Option II/III once exercised should not be changed in financial year
- Prior intimation for Option III
- Balance as on 1 April 2008
  - whether available if following Option I/II/III?
  - Tungabhadra Industries Limited vs. Union of India 118 ELT 545 (SC)
- Option III
  - Whether any other proportion can be used?

## Some Issues:

Description	Nature	Amt. Payable	Numerator	Denominator
Services governed by Rule	TS	No	No	Yes
Export of Services	TS	No	No	Yes
Services to units located in SEZ	ES	Yes	Yes	Yes
Services rendered outside the territorial jurisdiction	None	No	No	No
Trading in Goods	None	No	No	No
Investment Incomes / Surplus	None	No	No	No
Prohibitions under other Notifications	ES?	Not Practical	Yes	Yes

Thank You for a patient hearing.

Awaiting Questions from the Floor..