Chapter V

Effectiveness of Internal Controls

5.1 Internal Control

Internal control is an integral process carried out by an entity's management and personnel which is designed to address risks and provides reasonable assurance that following general objectives are achieved:

- executing orderly, ethical, economical, efficient and effective operations;
- fulfilling accountability obligations;
- complying with applicable laws and regulations;
- safeguarding resources against loss, misuse and damage.

5.2 Audit findings

Central Excise Department exercise internal controls by way of two functions i.e. Scrutiny of Returns and Internal Audit. We found from test check of records, 56 cases of failure of internal control, having revenue implication of ₹ 104.68 crore, which are illustrated below.

5.3 Non-Conduct of Internal Audit

We noticed 9 cases, where Internal Audit was due but not conducted by the Department, which are illustrated below.

5.3.1 Short Payment of Central Excise Duty

5.3.1.1 Short Payment of Duty Due to Undervaluation

As per section 4(1)(b) of Central Excise Act, 1944, read with Rule 7 of Central Excise (Valuation) Rules, 2000, where the excisable goods are not sold by the assessee at the time and place of removal but are transferred to a depot, premises of a consignment agent or any other place or premises (hereinafter referred to as "such other place") from where the excisable goods are to be sold after their clearance from the place of removal and where the assessee and the buyer of the said goods are not related and the price is the sole consideration for the sale, the value shall be the normal transaction value of such goods sold from such other place at or about the same time and, where such goods are not sold at or about the same time, at the time nearest to the time of removal of goods under assessment.

M/s. Esquire Multiplast Pvt. Ltd., Kalamasserry, under Cochin Commissionerate, engaged in manufacture of plastic furniture, toys, articles of conveyance and packing goods of plastic sold these goods through the factory gate as well as through their depots. The assessee was paying Central Excise duty for all clearances including that from depots, on the basis of value as per invoices issued from the factory. The goods transferred to the depots were sold at a higher price and the average depot price was higher than the invoiced price for sale from factory by 8.47 per cent. As per trial balance for the year 2012-13, value of clearance of depot was ₹ 16.67 crore and value of goods cleared from depot was ₹ 18.08 crore. This resulted in undervalue of goods and short payment of duty of ₹ 17.45 lakh.

Though the assessee fell in biennial category for Internal Audit, no Internal Audit was conducted since December 2011.

When we pointed this out (March 2014), the Ministry admitted the observation (September 2016) and stated that the assessee had deposited amount of ₹ 18.87 lakh with interest of ₹ 3.62 lakh. On the lapse of Internal Audit, it stated that audit was not conducted due to manpower constraints.

5.3.1.2 Short Payment of Excise Duty

Rule 8 of Central Excise Rules, 2002, provides that Central Excise Duty should be paid on monthly basis by 5th day of succeeding month, (6th day of the following month in case of e-payment through internet banking) except for the month of March, when duty is to be paid by 31st March. Further, as per Rules 8 (3A) of the above mentioned rule as amended vide notification no. 19/2014-CE (NT) dated 11 July 2014, if the assessee fails to pay the duty declared as payable by him in the return, within a period of one month from the due date, then the assessee is liable to pay the penalty at the rate of one percent, on such amount of the duty not paid, for each month or part thereof calculated from the due date, for the period during which such failure continues.

Audit examination of records along with ER-1 returns of M/s Trading Engineers (International) Ltd Unit-II, Lakeshwari, Roorkee under Dehradun Commissionerate, revealed (May 2016) that during the month of March 2016, the assessee cleared finished goods having assessable value of ₹ 11.01 crore on which Central Excise duty of ₹ 1.38 crore was payable. We noticed that the assessee paid excise duty of ₹ 34.55 lakh only, during the month of March 2016. Thus, the assessee short paid excise duty, to the extent of ₹ 1.03 crore.

Although this unit was to be mandatorily covered under Internal Audit, the Internal Audit Wing of the Department did not conduct audit during 2015-16.

When we pointed this out (May 2016), the Ministry stated (October 2016) that the assessee has deposited the excise duty of ₹ 1.03 crore along with interest of ₹ 2.08 lakh and penalty of ₹ 2.06 lakh. On not conducting of Internal Audit, it stated that unit was audited upto November 2014 and selected for next audit in November 2016.

5.3.2 Irregular Availing of CENVAT Credit

5.3.2.1 Irregular Availing of CENVAT Credit on Input

As per Rule 2(k) of CENVAT Credit Rules, 2004, "input" means all goods used in the factory by the manufacturer of the final products. Sub-rule (k) of the Rule defines "Final products" as excisable goods manufactured or produced from input, or using input service. Further Rule 3(1) of CENVAT Credit Rules, 2004 allows a manufacturer of final products to take credit of specified duties paid on inputs.

M/s. Baramati Agro Ltd., in Pune III Commissionerate, manufactured both excisable products viz. Sugar, Molasses and Denatured Ethyl Alcohol falling under chapter heading 17 and 23 of CETA 1985 and non-excisable products such as Rectified Spirit, Extra Neutral Alcohol (Un-denatured Ethyl Alcohol and Un-denatured Spirits). Scrutiny of records revealed that the assessee manufactured non-excisable goods from both captively consumed Molasses and Molasses purchased from outside parties. Further scrutiny revealed that the assessee availed CENVAT credit on the duty paid on Molasses purchased from outside parties. As the Molasses were used for the manufacturing of non-excisable goods, the availment of CENVAT credit on the purchased Molasses was not in order, in view of above mentioned provisions.

Further, during the verification of records of Range V (Walchand Nagar) of the said Commissionerate, audit noticed that SCN of ₹ 14.95 crore was issued to the assessee in December 2014, covering the period from November 2009 to March 2014, for payment of duty for denial of exemption under notification on captively consumed Molasses, on the ground that these Molasses were used for manufacturing non-excisable goods i.e. Rectified Spirit, Extra Neutral Alcohol. It was also noticed that the unit being the mandatory unit for audit, it was not audited for the period from 2012-13 to 2014-15.

When we pointed this out (September 2015), the Ministry contested the observation and stated (December 2016) that similar issues have been decided by CESTAT and Karnataka High Court. On the lapse of internal audit, it stated that internal audit could not be completed due to time constraints.

If the decision of Karantaka High Court is accepted by the Ministry, the same needs to be clarified to all field formations for similar compliance.

5.3.2.2 Irregular Availing of CENVAT Credit on Input Services

As per Rule 2 (1) of CENVAT Credit Rules, 2004, following services have been excluded from the purview of the definition of 'input service':

(i) Service portion in the execution of works contract and construction services, including service listed under clause (b) of section 66E of the Finance Act, 2004, in so far as they are used for construction or execution of works contract of a building or a civil structure or a part thereof or laying of foundation or making of structure for support of capital goods

(ii) Service provided by way of renting of a motor vehicle, in so far as they relate to a motor vehicle which is not a capital goods

(iii) Service of general insurance business, servicing, repair and maintenance, in so far as they relate to a motor vehicle which is not a capital goods and

(iv) Such as those provided in relation to outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, membership of a club, health and fitness centre, life insurance, health insurance and travel benefits extended to employees on vacation such as leave of home travel concession, when such services are primarily used for personal use or consumption of an employee.

Audit examination of records of M/s Indian Oil Corporation Ltd. Refinery Division, Barauni, in Patna Commissionerate revealed (March 2016) that the assessee availed and utilised CENVAT credit of ₹ 23.35 lakh during 2014-15 on Service Tax paid for civil works e.g. barricading, construction of rooms, renovation of canteen. Administrative buildings and toilets, repair and maintenance, painting works and maintenance of garden etc. Since all these services do not fall within the definition of the input service, CENVAT credit of Service Tax paid on these services, was not admissible.

Although M/s Indian Oil Corporation Ltd. Barauni was a mandatory unit, the Internal Audit of the Commissionerate, did not conduct audit for the period 2014-15.

When we pointed this out (March 2016), the Ministry admitted the observation (November 2016) and stated that SCN for 23.59 lakh had been issued. On not conducting of the Internal Audit, it stated that Audit Commissionerate, Patna had planned to conduct audit of the unit in 2016 covering the period of 2014-15 also.

5.3.2.3 Irregular Availing of CENVAT Credit on Ineligible Documents

Rule 3(1) read with Rule 9 of the CENVAT Credit Rules, 2004 prescribes the conditions and documents, on which a manufacturer or producer of final

products or provider of output service, shall be allowed to take credit of duties specified there under, paid on any input or capital goods received in the factory of manufacturer of final product or premises of the provider of output service.

M/s Corrtech International (P) Ltd., a service provider falling under jurisdiction of Ahmedabad Service Tax Commissionerate, availed CENVAT credit (August 2010 to October 2012) of capital goods, without documents, as specified in CENVAT Credit Rules, 2004. This resulted into irregular availment of CENVAT credit to the tune of ₹ 14.94 lakh.

Preventive wing of the Department, visited the assessee premises and covered period upto August 2013, but failed to detect the issue. Moreover, audit of the assessee has not been conducted by the Department in due time.

When we pointed this out (March 2015), the Ministry admitted the observation (December 2016) and stated that the assessee had reversed the CENVAT credit of ₹ 14.94 lakh. It further stated that preventive wing is restricted to specific issues relating to intelligence/information available, it can not be equated to audit. It further stated that unit was not selected for audit due to preventive investigation and shortage of staff.

5.3.2.4 Irregular Availing of CENVAT Credit of Education Cess and Secondary and Higher Education Cess

(vi) Rule 3(1) of CENVAT Credit Rules, 2004 provides that a manufacturer of final products shall be allowed to take credit of specified duties paid on any input or capital goods received in factory of manufacturer of final products on or after 10 September 2004.

Government of India vide notification number 13/2012-Customs and 14/2012-Customs, dated 17 March 2012, exempted the imported goods from payment of Education cess and Secondary and Higher Education cess, leviable under sub-section (1) of section 3 of the Customs Tariff Act, 1975.

In Range IV under Haldia-II Division of Haldia Commissionerate, checking of returns revealed that M/s Ennore Coke Ltd. availed CENVAT credit of Education cess and Secondary and Higher Education cess on imported inputs during April 2013, September 2013 and November 2013, which was exempted vide notifications ibid. This resulted in irregular availing of CENVAT credit of ₹ 12.49 lakh which was recoverable from the assessee, along with applicable interest.

Further, the assessee is a mandatory unit and was to be covered annually in Internal Audit, as per Departmental norms. But the Department did not audit

the assessee since March 2013. Thus, the lapse remained undetected until pointed out by CERA.

When we pointed this out (March 2015), the Ministry admitted the observation (November 2016) and stated that the assessee had reversed the CENVAT credit of 12.49 lakh with interest of ₹ 4.32 lakh. On the lapse of Internal Audit, it stated that audit was not conducted, due to manpower constraints.

5.3.3 Short Reversal of CENVAT Credit

According to Rule 6 (2) of CENVAT Credit Rules, 2004, manufacturer availing CENVAT credit of inputs or input services and manufacturing such final products which are chargeable to duty as well as exempted goods, shall maintain separate accounts for receipt, consumption and inventory of inputs and input services and take CENVAT credit only on that quantity of input or input service, which are intended for use in the manufacture of dutiable goods. Rule 6(3) states that the manufacturer, opting not to maintain separate accounts, shall either pay an amount equal to six per cent of value of exempted goods and services; or pay an amount as determined under sub-rule (3A). Sub-rule (3A) stipulates provisional reversal of CENVAT credit by the manufacturer in each month and at the end of the financial year, actual reversal of CENVAT credit attributable for manufacturer of exempted goods.

M/s Cipla Ltd. Kumrek in Siliguri Commissionerate manufactured both dutiable and exempted pharmaceutical products availing credit on common inputs and input services. The assessee opted not to maintain separate accounts for inputs and input services and thus exercised option (ii) of rule 6(3) of CENVAT Credit Rules, 2004. In each month the assessee provisionally paid the amounts under the said rule and at the end of the financial year, determined and paid the differential amount. During the year 2013-14, the assessee availed CENVAT credit of ₹ 590.29 lakh on input services on which proportionate credit of ₹ 38.66 lakh was to be reversed. The assessee provisionally reversed ₹ 7.28 lakh and at the end of the year determined the amount of input service credit attributable to exempted goods as per the formula u/r 6(AS) and reversed an amount of ₹ 1.83 lakh, although the assessee was actually liable to pay differential amount of ₹ 31.38 lakh. This resulted in short reversal of CENVAT credit of ₹ 29.55 lakh, which was recoverable from the assessee along with interest as applicable.

The assessee is a mandatory unit and to be annually audited but the unit was not audited by the Department since December 2013. Thus, the lapse remained undetected until pointed out by CERA.

When we pointed this out (March 2015), the Ministry admitted the observation (November 2016) and stated that SCN for ₹ 52.05 lakh had been issued to the assessee. On the lapse of Internal Audit, it stated that audit was not conducted due to manpower constraints.

5.3.4 Non/Short Payment of Interest

5.3.4.1 Non-Payment of Interest

Rule 3 of Section the CENVAT Credit Rules, 2004 allows a manufacture or provider of output service to avail CENVAT credit of Central Excise duty/ Service Tax paid on inputs, capital goods or input service provided that said inputs, capital goods, input service should be used in manufacture of dutiable products or providing taxable output service. Further, Rule 14 of the CENVAT Credit Rules, 2004 provides that interest is liable to be paid on wrongly availed and utilized CENVAT credit.

M/s. Jai Corp Limited, under Commissioner of Central Excise, Daman, reported loss of plant and machineries, stock of raw materials, finished goods etc., due to fire, which broke out in the factory on 11 October 2012 and intimated details of credit availed on the inputs and capital goods destroyed in fire, vide its letter dated 8 October 2013. CENVAT credit of ₹ 2.66 crore, involved in the goods destroyed in the fire, was paid by the assessee on 7 October 2013 through PLA and CENVAT account, after a period of around one year. However, the assessee did not pay applicable interest on the belated reversal of CENVAT credit, availed and utilized.

Moreover, audit of assessee was not conducted by the Department in due time.

When we pointed this out (July 2015), the Ministry admitted the observation partially (November 2016) and stated that interest actually payable was ₹ 38.34 lakh which has been paid by the assessee. For not conducting the Internal Audit, no reply was furnished by the Ministry.

5.3.4.2 Short Payment of Interest

According to Notification No. 46/2001 CE (NT) dated 26 June 2001, Central Government extended the facility of removal of excisable goods from the factory of production to a warehouse, without payment of duty. As per para 10.3 of CBEC Circular No. 581/18/2001 CX dated 29 June 2001 read with Notification No. 46/2001-Central Excise (NT) dated 26 June 2001, when goods were diverted for home consumption with the permission of jurisdictional Deputy/Assistant Commissioner, interest should be paid at the rate of 24 per cent per annum on the duty payable, calculated from the date of clearance

from the factory of production, till the date of payment of duty and clearance.

M/s. Bharat Petroleum Corporation Ltd. – Kochi Refinery (BPCL-KR), under Cochin Commissionerate, cleared 8958 KL of HVFO (Furnace Oil) to Bunkering Terminal, Jawaharlal Nehru Port Trust, Sheva, Navi Mumbai, for export warehousing. This was intended for sale as bunker fuel for vessels on foreign run/voyage. Out of the 8958 KL, quantities of 1025 KL and 3454 KL were diverted for home consumption on 13 February 2014 and 03 March 2015 respectively, by paying duty and interest. However, interest was paid at the rate of 18 per cent as against 24 per cent payable in the case of clearance of 3454 KL. This resulted in short payment of interest of ₹ 22.23 lakh.

Even though the assessee was a mandatory unit for Internal Audit, no Internal Audit was conducted since March 2014.

When we pointed this out (September 2015), the Ministry admitted the observation (September 2016) and stated that the assessee had deposited amount of ₹ 22.23 lakh. On the lapse of Internal Audit, it stated that audit was not conducted due to manpower constraints.

5.4 Incomplete Coverage of Period by Internal Audit

Central Excise Audit Manual 2008, stipulates that audit should extend upto one completed month preceding the date of current audit. We noticed 2 cases where audit was not extended to the adequate period, which are illustrated below.

5.4.1 Irregular Availing of CENVAT Credit on Invalid Documents

Rule 9 of CENVAT Credit Rules, 2004 read with notification no. 26/2014-C.E.(N.T.) dated 27 August 2014, provided that CENVAT credit shall be allowed on a Service Tax Certificate for Transportation of goods by Rail (STTG Certificate) issued by the Indian Railways, along with the photocopies of the railway receipts mentioned in the STTG Certificate.

M/s Maithan Alloys Ltd and M/s Impex Ferro Tech Pvt. Ltd. in Bolpur Commissionerate, availed CENVAT credit of ₹ 9.39 lakh and ₹ 6.05 lakh respectively during August 2014 to March 2015, on the basis of photocopy of Railway receipt but did not have the statutory STTG Certificates required for such credits. This resulted in irregular availing of CENVAT credit of ₹ 15.44 lakh, which was recoverable along with interest.

Both the assessees were mandatory units and Department audited the first unit during May 2015 and second unit during March 2015, both covering the period 2013-14, although the provisions of Central Excise Audit Manual 2008,

stipulates that audit should extend up to one completed month preceding the date of current audit. The lapse remained undetected until pointed out by CERA.

When we pointed this out (September 2015), the Ministry while accepting the observation intimated (December 2016) that irregularly availed credits were reversed by the assessees in September 2015. Further, it stated that the auditors conducted the audit for the period as per the plan which was approved for 2013-14 and observation raised by CERA pertains to 2014-15. It further added that the objection of CERA has been noted for future guidance.

The reply of the Ministry as regards to the non-coverage of the issue by the internal audit is not acceptable as Central Excise Manual 2008, stipulates that audit should extend upto one completed month, preceding the date of current audit.

5.4.2 Non-Reversal of CENVAT Credit

Rule 6(3) of the CENVAT Credit Rules, 2004 provides that if CENVAT credit is availed on common inputs/input services, which are used in manufacture of exempted goods as well as in dutiable goods and separate accounts for inputs are not maintained, then the manufacturer shall either pay an amount equivalent to six per cent (five per cent upto 31 March 2012) of value of the exempted goods or pay an amount equivalent to the CENVAT credit attributable to inputs and input services used in or in relation to the manufacture of exempted goods or provision of exempted services.

M/s Dabur India Ltd., in Kolkata-V Commissionerate (under erstwhile Kolkata-VII Commissionerate) cleared the exempted goods Honey/ Madhu amounting to ₹ 14.39 crore during 2011-12 using common input services like BAS, Management Consultant Services, CFA services etc. for the manufacture of said exempted goods. However, the assessee neither maintained separate accounts for inputs and/or input services nor paid amount equivalent to six/five per cent of the value of the exempted goods. This resulted in non-payment of ₹ 71.95 lakh which is recoverable along with interest at applicable rates.

The assessee was a mandatory unit and was audited by Internal Audit in December 2011. Provisions of Central Excise Audit Manual 2008, stipulates that audit should extend upto one completed month preceding the date of current audit. However, the lapse remained undetected until pointed out by CERA.

When we pointed this out (August 2012), the Ministry while accepting the observation intimated (December 2016) that three show cause notices have been issued periodically covering the entire period of lapse and out of these,

in two SCNs demand have been confirmed. As regards failure of Internal audit, it stated that internal audit was conducted for the period 2011-12 in December 2012, during which the subject issue was detected and necessary action in form of SCNs was initiated.

The reply of the Ministry is not relevant to the audit observation as audit pointed out non-detection of issue during the internal audit conducted in December 2011.

5.5 Non-Detection of Assessees' Lapses by Internal Audit

We noticed 41 cases where Internal Audit was conducted by the Department but they failed to detect the lapses committed by the assessees, which are illustrated below.

5.5.1 Non-payment of Duty

5.5.1.1 Non-payment of Differential Duty

According to Rule 4 of Central Excise Rules, 2002, every person who produces or manufactures any excisable goods, shall pay duty leviable on such goods in the manner provided in Rule 8. Rule 6 states that the assessee shall himself assess the duty payable on any excisable goods. As per Rule 5, the rate of duty, applicable to any excisable goods, shall be the rate in force on the date, when such goods are removed from factory. Section 11 A (1) (b) (i) of Central Excise Act 1944 stipulated that, where any duty of excise has not been levied or paid or has been short levied or short paid or erroneously refunded, for any reason other than fraud or collusion etc., the person, chargeable with the duty may, before service of notice under clause (a), pay on the basis of his own ascertainment of such duty; the amount of duty along with interest payable thereon under section 11 AA.

M/s. Traco Cables Co. Ltd., a Central Excise assessee in Cochin Commissionerate, manufacturing Electrical wires, cables, telephone cables etc., did not pay an amount of ₹ 25.81 lakh being differential duty which became payable on account of upward revision of sale price of goods, sold to Kerala State Electricity Board (KSEB) and M/s. BESCOM, during the period 2013-14 to 2014-15. Interest was also payable.

Even though Internal Audit covering the period up to March 2014 was conducted in July 2014, the lapse detected by CERA was not found out.

When we pointed this out (August 2015), the Ministry admitted the observation (October 2016) and stated that the assessee had paid (September 2015 and November 2015) differential duty of ₹ 25.81 lakh along with interest of ₹ 5.32 lakh. On the lapse of Internal Audit, it stated that Audit

was conducted for the period April 2013 to March 2014, while most of the sales of goods, amounting to 23.80 lakh, as reflected in CERA audit observation, took place between April 2014 to November 2014. Sale of only ₹ 2.02 lakh pertained to the period covered by Internal Audit. However, clarification had been sought from the Internal Audit Party regarding non-detection of the lapse.

5.5.1.2 Non-Payment of Duty on Clearance of Capital Goods

Rule 3(5) of the CENVAT Credit Rules provide that if the capital goods on which credit has been taken are removed after being used, the manufacturer or provider of output service 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. Further, if the capital goods are waste and scrap, the manufacturer shall pay an amount equal to the duty leviable on transaction value.

M/s Bilag Industries Ltd. (now Bayer Vapi Pvt. Ltd.) under Valsad Commissionerate, which used to avail CENVAT credit on its Capital goods, had shown 'Deletion of Plants and Machineries' amounting to a total ₹ 12.79 crore, in its Balance Sheet for the period 2008-09 to 2011-12. Since the audited entity had availed CENVAT credit on its capital goods, duty was required to be paid on their clearance as scrap or capital goods as such. However, it could not furnish evidence of any duty payment, made on the amount of the plant and machinery, deleted from its accounts. We brought this to the notice of the Department (December 2012) with a request to ascertain the actual amount of duty payable on the scrap and above plant and machinery.

When we pointed this out (December 2012), the Ministry admitted the observation (November 2016) and stated that two SCNs issued to the assessee had been adjudicated, resulting in confirmation of demand of ₹ 1.67 crore. The assessee appealed in CESTAT, which was pending. On the lapse of Internal Audit, the Ministry stated that the explanation, called from the officers, would be examined for further action.

5.5.1.3 Non-payment of Duty on Intermediate Goods

Rule 12BB of Central Excise Rules, 2002, permits large taxpayers to remove excisable goods from one registered premises to another registered premises, without payment of duty, provided that the final products manufactured out of such intermediate products, are cleared on payment of duty, within a period of six months, from the date of receipt of intermediate goods, in the recipient premises. In case such final products are not cleared by the recipient premises within the stipulated period of six months, duty on the said intermediate goods shall be paid by the recipient with interest.

M/s Karnataka Soaps and Detergents Ltd. Bangalore, under Large Taxpayer Unit (LTU) Bangalore, procured sandalwood oil fraction from its Sandalwood Oil Division, Mysore, without payment of duty under Rule 12BB ibid, for manufacture of final products. Audit scrutiny revealed that out of 451.704 kg of oil (including opening balance of 114.904 kg as on 1st April 2012), received during the period upto August 2016, only 19.491 kg was utilised for manufacture, within the stipulated time of six months, 285.139 kg was utilised beyond six months and the balance of 147.074 kg was yet to be utilised (August 2016). As such, the assessee was liable to pay duty of ₹ 19.94 lakh alongwith interest on the unutilized oil, besides interest on oil utilised beyond six months. The Internal Audit Wing of the LTU, Bangalore did not detect this non-payment during its audit (July-September 2014), covering the period upto March 2014.

When we pointed this out (May 2015), the Ministry admitted the observation (November 2016) and stated that SCN for ₹ 19.94 lakh had been issued to the assessee. Ministry further stated that the assessee is complying with rule 12BB as the final product is being cleared within six months. Though, a residual quantity of sandalwood oil fraction is lying in stock beyond a period of six months, but it is only a procedural lapse, as if the duty is to be paid by the Mysore unit, the credit of the same can be availed by the Bangalore unit.

The reply is not tenable as the period of six months has been prescribed by the Board to give the manufacturer ample time to clear the manufactured goods. The assessee should follow the procedure beyond this period and Department should ensure compliance, even if the process is revenue neutral.

5.5.1.4 Non-Payment of Duty on Clearance of Exempted as Well as Dutiable Goods

As per Rules 6(2) of the CENVAT Credit Rules, 2004 where a manufacturer or provider of output service avails CENVAT credit in respect of any inputs or input services and manufacturers such final products or provides such output service which are chargeable to duty or tax as well as exempted goods or services, then the manufacturer or provider of output service maintain separate accounts for receipt, consumption and inventory of input and input service, meant for use in the manufacture of dutiable final products or in providing output service and the quantity of input meant for use in the manufacture exempted goods or services. Further, as per rule 6(3) if the assessee does not maintain a separate account, then the assessee has to pay an amount equal to 5 per cent up to (16 March 2012) and 6 per cent from 17 March 2012 of the value of the exempted goods.

M/s Domino Printech India Ltd. Plot No. 299 Sector 6, IMT Manesar, Gurgaon was engaged in the manufacturing of Printing-ink-reseroir, Printing-ink-cartridge, printing ink content, printing ink made-up-cartridges and wash-solution under chapter head 32159090 and 29141990. During preliminary scrutiny of ER-I for the year 2011-12 and 2012-13, it was noticed that the assessee was manufacturing and clearing dutiable as well as exempted goods and no separate account was maintained of common input used in or in relation to manufacturing of dutiable and exempted goods. The assessee cleared exempted goods valuing ₹ 27.45 crore in 2011-12 and ₹ 31.11 crore in 2012-13, but the assessee did not pay the duty amounting to ₹ 1.37 crore (₹ 27.45 crore X 5 per cent) in 2011-12 and ₹ 1.86 crore (₹ 31.11 crore X 6 per cent) in 2012-13. This resulted into non-payment of duty to the tune of ₹ 3.24 crore. Internal Audit, though carried out for the period 2011-12 and 2013-14, had not pointed out the lapse, detected by CERA.

When we pointed this out (November 2013), the Ministry while not accepting the observation, intimated (December 2016) that the inputs used for manufacture of dutiable and exempted goods are different. Therefore, the assessee is not availing CENVAT credit on inputs used in exempted goods.

The reply of the Ministry is silent on the aspect of non detection of the lapse by the internal audit and obligation on the part of assessee to maintain separate accounts.

5.5.2 Short Payment of Duty

5.5.2.1 Short Payment of Duty Noticed Due to Discrepancies in the Sales Amount

According to sub-section 1(a) of Section 3 of the Central Excise Act, 1944, Central Excise duty shall be levied and collected on all excisable goods which are produced or manufactured in India as, and at the rates, set forth in the First Schedule to the Central Excise Tariff Act, 1985.

M/s Bilag Industries Pvt. Ltd. (now Bayer Vapi Pvt. Ltd.), under Valsad Commissionerate, was having a DTA unit and a hundred per cent EOU unit at Vapi for which it was maintaining a consolidated balance sheet. We noticed that Balance Sheet and ER-1 returns of the audited entity depicted abnormal variations in the sales figures (including export of the units) as detailed below:

Table 3.1: Sales as per Balance Sheet

(Amount in ₹)

Year	2008-09	2009-10	2010-11	2011-12
Domestic Sales	2,02,45,92,104	2,02,16,42,330	2,38,32,02,414	885,60,00,000 (Bifurcation not given)
Export	6,45,97,74,670	5,86,79,62,966	5,08,58,30,464	
Total	8,48,43,66,774	7,88,96,05,296	7,46,90,32,878	885,60,00,000

Table 3.2: Sales as per ER-1

(Amount in ₹)

Year	2008-09	2009-10	2010-11	2011-12
Domestic Sales	1,74,65,89,247	1,49,29,98,057	1,79,39,88,348	2,13,93,36,279
Export	3,14,99,37,217	3,60,93,29,323	3,71,93,05,348	4,37,04,79,245
Total	4,89,65,26,464	5,10,23,27,380	5,51,32,93,696	6,50,98,15,524

The assessee could not provide reconciliation of the discrepancy in sales figures of Balance Sheet with the ER-1 and ER-2 returns. Department was requested (December 2012) to verify the discrepancy noticed and recover the differential duty payable, if any.

Internal Audit was conducted for the period upto 2011-12 but failed to detect the observation noticed by the CERA audit.

When we pointed this out (December 2012), the Ministry admitted the observation (November 2016) and stated that the demand of ₹ 7.62 crore had been confirmed (March 2016). Assessee's appeal against the order was pending in CESTAT. Ministry further stated that lapse on the part of Internal Audit was regretted and explanation will be sought from the concerned officer.

5.5.2.2 Short Payment of Duty Due to Incorrect Rate of Duty

(i) Sl. No. 292A of Notification No.12/2012-CE dated 17 March 2012, as amended by Notification No.12/20013-CE dated 1 March 2013, prescribes 14 per cent basic excise duty on clearance of bus chassis and other goods falling under Tariff item 87060029.

M/s Volvo India Pvt. Ltd. Bangalore, a large taxpayer unit in LTU Bangalore Commissionerate, manufactures tippers, tractors, trailers and chassis falling under Chapter 87 of the First Schedule of Central Excise Tariff Act, 1985. Audit of the Central Excise records of the assessee revealed that the assessee

cleared bus chassis under Tariff item 87060029 by paying basic excise duty at the rate of 13 per cent instead of at 14 per cent, during the period from March 2013 to December 2013 on assessable value of ₹ 28.95 crore, resulting in short payment of duty (including cess) of ₹ 29.82 lakh.

Though the Internal Audit Wing of the Large Taxpayers Unit, Bangalore audited the unit twice (during June-July 2013 and September-October 2015), this short payment of duty was not detected.

When we pointed this out (January 2016), the Ministry stated (October 2016) that the assessee paid duty of ₹ 29.82 lakh and interest of ₹ 13.76. On the lapse of Internal Audit, the Ministry stated that Internal Audit was conducted during June-July 2013 and covered the period upto March 2013, hence, the short payment was not detected. Subsequent Internal Audit for the period April 2013 to March 2015 was finalized in March 2016. As, CERA audit was conducted in January 2016 and short payment of duty was already covered by it, same was not included by Internal Audit.

The reply of the Ministry is not tenable as Internal Audit for the period April 2013 to March 2015 was completed on 8 October 2015 which failed to detect and the short payment was not detected. Only, the meeting of monitoring committee was conducted in March 2016 to discuss and finalise the audit observation.

Thus, Internal Audit not only failed to detect the lapse of the assessee, it also tried to give wrong facts to hide its lapse. Ministry may examine the facts and suitable action may be taken against the erring officials.

(ii) As per Rule 5 of Central Excise Rules 2002, the rate of duty of tariff value applicable to any excisable goods, shall be the rate or value in force on the date when such goods are removed from a factory or a warehouse, as the case may be.

During the course of audit of Central Excise records of the office of the Superintendent of Central Excise, Gandhinagar Range, it was noticed from the ER-1 returns of M/s Nucon Aerospace Pvt. Ltd., for the period from February 2014 to April 2014, that the assessee paid central excise duty at the rate of 10.30 per cent, instead of at the rate of 12.36 per cent, on the goods falling under CETSH-84792090. This incorrect application of rate of duty, resulted in short payment of duty of ₹ 41.62 lakh (as detailed in Addendum-V) which needs to be recovered from the assessee along with interest.

Though the ACES had thrown this error in Preliminary scrutiny, the Department did not initiate any action. Further, this aspect was not noticed by the Department, even in the Internal Audit during August 2014.

When we pointed this out (July 2015), the Ministry, while accepting the observation, stated (December 2016) that the assessee have paid duty of ₹ 41.62 lakh along with interest of ₹ 14.02 lakh. On the lapse of internal audit, the Ministry stated that issue could not be detected due to randomly selected months. Further, it stated that assessee suppressed the information while filing his returns.

5.5.2.3 Short Payment of Duty on Clearing Used Capital Goods

Rule 3(5) of the CENVAT Credit Rules provide that if the capital goods on which credit has been taken, are removed after being used, the manufacturer or provider of output service, 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. As per proviso under Rule 3(5A) of CENVAT Credit Rules, 2004, if the amount calculated under Rule 3(5A) (b) of the rule ibid, 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.

M/s Shree Cement Limited (Grinding Project), Bhiwadi in Alwar Commissionerate, has cleared old & used machineries on transaction value ₹ 6.09 crore, for which an amount of ₹ 75.30 lakh was required to be paid as per proviso of rule ibid, whereas the assessee paid an amount of ₹ 49.69 lakh as per calculation of rule 3(5A) (b) of CENVAT Credit Rules, 2004. This resulted in short payment of ₹ 25.62 lakh.

Internal Audit, though carried out up to May 2014, covering the period, but did not point out the lapse detected by CERA.

When we pointed this out (November 2015), the Ministry contested the observation (November 2016) and stated that capital goods was not sold but merely transferred to the sister unit, hence, concept of transaction value was not applicable and duty payable was correct as per rule 3(5A) (a) (ii).

The reply is not tenable as the assessee issued invoice for removal of capital goods to its own unit, thus declaring a transaction value. Hence, assessee was required to arrive at the amount payable, by following rule 3(5A)b.

5.5.2.4 Short Payment of Duty Due to Undervaluation

Section 4 of the Central Excise Act defines 'transaction value' as the price actually paid or payable for the goods, when sold, including any amount that the buyer was liable to pay to, or on behalf of, the assessee, by reason of, or in connection with the sale. Rule 6 of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 stipulates that when the price is not the sole consideration for sale, the value for Central Excise purpose, of such goods should be deemed to be the aggregate of such transaction value and

the amount of money value of any additional consideration flowing directly or indirectly from the buyer to the assessee.

(i) M/s Swastik Copper Pvt. Ltd., in Jaipur Commissionerate is engaged in manufacture and maintenance of Transformers. The assessee made a contract for repair of transformer making provision to deduct value of scrap emerged during repairs from the total cost of repaired transformers. Accordingly, the assessee adjusted the cost of scrap amounting to ₹ 1.69 crore during 2012-13 to 2014-15 in the invoices before payment of the excise duty, which resulted in suppression of assessable value to the extent of cost of scrap. This resulted in short payment of duty of ₹ 20.05 lakh which was recoverable with interest.

Internal Audit of the assessee was carried out up to March 2014, partially covering the period mentioned in observation, but it failed to detect the lapse.

When we pointed this out (May 2015), the Ministry admitted the observation (September 2016) and stated that the assessee had deposited duty of ₹ 20.05 lakh with interest of ₹ 6.17 lakh. On the lapse of Internal Audit, the Ministry stated that the explanation was being called for from the concerned audit officer.

(ii) M/s Jindal Aluminium Ltd. Bangalore in Bangalore LTU Commissionerate, manufactures customer specific dies for articles as per the customers' requirements. The customers are bound to purchase the stipulated minimum quantity within the stipulated period. The quotation issued by the assessee states that cost of development of new section will be charged as 'security for new die', which will be forfeited, in case the assessee fails to purchase the minimum specified quantity of the articles, within the stipulated time. Thus, the forfeited amount is towards the cost of dies and in relation to the sale and should have been considered as an additional consideration, flowing directly from the buyer to the assessee. Although the assessee realised an amount of ₹ 8.46 crore, by way of forfeiture of security deposits, during the years from 2010-11 to 2013-14, the assessee did not include this amount in the assessable value, which resulted in short payment of Central Excise duty and cess of ₹ 96.43 lakh during the said period.

Though the Internal Audit was carried out by the Department, covering the period 2010-11 to 2013-14, the lapse remained undetected until pointed out by CERA audit.

When we pointed this out (December 2014), the Ministry stated (November 2016) that forfeited charges are in the nature of liquidated

damages wherein the large taxpayer is compensated for the die manufacturing charges, when customer fails to lift the agreed quantity of extrusion. The security deposit collected, is not the cost of the die and to be refunded to the customer, if agreed quantity is taken delivery by the customer. Ministry further stated that the CESTAT decision in case of M/s Jindal Praxair Oxygen Co. Ltd. [2007 (208) ELT 181 (Tri. Bang)] was also applicable in the present case.

The reply is not tenable as the terms and conditions for supply of new dies specified that the security deposit is collected towards tooling charges, incurred for development of customer-specific sections/dies. Since these additional charges are directly related to sale, the same cannot be considered either as liquidated damages or as service charges liable to Service Tax. The CESTAT decision in the case of M/s Jindal Paraxair Oxygen Co. Ltd. is not applicable in the present case as the decision was on the basis of 'normal wholesale price' concept and the valuation rules which existed prior to July 2000, while the present case is based on Valuation rules which came into existence from 1 July 2000.

(iii) M/s Mahanadi Coalfields Ltd (MCL), in Rourkela Commissionerate who is a producer of coal (Chapter heading 27), received ₹ 19.46 crore in March 2011, as additional consideration (Performance Incentive) from its customers. However, the assessee did not include this additional consideration in the assessable value, resulted in non-levy of Central Excise duty of ₹ 1 crore which was recoverable with interest of ₹ 46.31 lakh.

Even in the Internal Audit by the Department, lapse was not detected.

When we pointed this out (February 2013), the Ministry admitted the observation (November 2016) and stated that demand of ₹ 1 crore had been confirmed with applicable interest. On the lapse of Internal Audit, it stated that issue was not detected due to audit being test check basis.

5.5.2.5 Short Payment of Duty Due to Undervaluation of Goods

Rule 5 of Central Excise valuation (Determination of price of excisable goods) Rules, 2000, provides that where excisable goods sold in the circumstances specified in clause (a) of sub-section (1) of section 4 of the Act except the circumstances in which the excisable gods are sold for delivery, at a place other than the place of removal, then the value of such excisable goods shall be deemed to be the transaction value, excluding the cost of transportation from the place of delivery of such excisable goods. Further, explanation 2 below the said rule clarified that the cost of transportation from the factory to the place of removal, where the factory is not the place of removal, shall not be excluded for the purposes of determining the value of the excisable

goods. Rule 6 of the valuations rules provides that in case, where price is not the sole consideration for the sale, but other requirement clause (a) of sub section (1) of section-4 of the Act are satisfied, the value shall be determined in accordance with the provisions of Rule 6 of the valuation rules.

(i) M/s Dynamic Cables Pvt. Ltd., Jaipur in Jaipur Commissionerate, executed agreements with Vidyut Vitran Nigams/ Railways etc. for supplying of Cables/ Conductors on FOR destination basis. Price was inclusive of packing and forwarding charges, Excise Duty, VAT and freight and insurance charges for delivery of materials at buyer's Stores. We noticed that the assessee received a sum ₹ 4.06 crore during 2011-12 to 2014-15 towards freight and insurance charges from buyers which were not included in assessable value of goods for payment of Excise duty. Thus, assessee undervalued the goods by ₹ 4.06 crore, resulted in short payment of duty ₹ 48.64 lakh.

Internal Audit, though conducted up to August 2014, partially covering the period, mentioned in CERA Audit observation, failed to detect the lapse.

We pointed this out in February 2016. In reply, Commissionerate intimated (April 2016) that SCN for ₹ 48.64 lakh has been issued.

When we pointed this out (February 2016), the Ministry admitted the observation (September 2016) and stated that SCN for ₹ 48.64 lakh with interest and penalty had been issued to the assessee. On the lapse of Internal Audit, the Ministry stated that the explanation was being called for from the concerned audit officer.

(ii) M/s ShriShakti Cylinders Pvt. Ltd., in Hyderabad-IV Commissionerate, engaged in the manufacture of LPG Cylinders falling under Chapter-73 of CETA-1985, supplied LPG Cylinders to M/s Indian Oil Corporation Ltd. Mumbai, M/s Hindustan Petroleum Corporation Ltd, Mumbai and M/s Bharat Petroleum Corporation Ltd, Mumbai during 2013-14 and 2014-15. It was observed from purchase orders and sale invoices that the assessee had cleared the above said goods on FOR destination basis. Hence, the title in goods would be passed to the buyer only on delivery of goods at destination. Therefore, the assessable value should include transportation charges and transit insurance charges, if any. However, the assessee discharged excise duty only on the cost of the goods, excluding freight charges incurred. Thus, non-inclusion of outward freight charges of ₹ 1.79 crore in assessable value, resulted in short payment of duty of ₹ 22.17 lakh which needs to be recovered from the assessee along with interest.

Though Internal Audit was conducted upto March 2014, this aspect was not noticed.

When we pointed this out (February 2016), the Ministry admitted the observation (September 2016) but stated that issue was already known to the Department, as the issue was taken up for investigation before being pointed out by CERA Audit. Based on investigation of anti-evasion wing, SCN of ₹ 42.43 lakh was issued to the assessee in April 2016. Regarding failure of Internal Audit, it stated that there are divergent views in light of various judgments and issue involves interpretation of Law.

The reply is not tenable as the Department issued the SCN after being pointed out by CERA Audit in February 2016. Also, if there issue is subject to different interpretations, Ministry need to issue suitable clarification to end the ambiguity.

(iii) M/s Vidyut Control Systems Pvt. Ltd., in Hyderabad-IV Commissionerate, engaged in the manufacture of 'Instrument Transformers' falling under Chapter-85 of CETA 1985, had supplied goods to various customers viz. AP Transco, TS Transco, AP Genco, TS Genco, TNSEB, KPTCL and KSEB during 2011-12 to 2014-15. It was observed from sale invoices that the assessee had quoted freight charges in addition to basis price of each item and cleared goods to above customers on the FOR destination basis and the risk of transportation and ownership of the goods rests with assessee, during the transport of the goods. Accordingly, the assessee had also received freight, insurance, forwarding and packing charges from the said customers. However, the assessee had not included the said amount in the assessable value for calculation of excise duty, as required under the above provisions. This resulted in short payment of excise duty ₹ 21.97 lakh (i.e. duty of ₹ 15.25 lakh and interest of ₹ 6.73 lakh, calculated up to 31 January 2016) which needs to be recovered from the assessee.

Though Internal Audit was conducted up to March 2014, this aspect was not noticed.

When we pointed this out (February 2016), the Ministry admitted the observation (September 2016) and stated that the assessee had paid ₹ 0.23 lakh with interest of ₹ 0.12 lakh and an SCN for ₹ 20.04 lakh with interest and penalty had also been issued. Regarding failure of Internal Audit, it stated that there are divergent views in light of various judgments and issue involves interpretation of Law.

The reply is not tenable as, if the issue is subject to different interpretations, The Ministry needs to issue suitable clarification to bring the ambiguity to a logical end.

5.5.2.6 Short Payment of Duty on Goods Cleared to Sister Unit

Rule 9 of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, as amended from 01 December 2013, stipulates that where the whole or part of excisable goods are sold by an assessee except to or through a person who is related in the manner specified in any of sub clauses (ii), (iii) or (iv) of clause (b) of sub section (3) of section 4 of the Act, the value of goods shall be the normal transaction value at which these are sold by the related person at the time of removal, to the buyers (not being related person) or where such goods are not sold to such buyers, to buyers (being related person), who sells goods in retail. Provided that in a case where the related person does not sell the goods but uses or consumes such goods in the production or manufacture of articles, the value shall be determined in the manner specified in rule 8 i.e. the value shall be one hundred and ten per cent of the cost of production or manufacture of such goods.

(i) M/s Mangala Product Private Limited, in Jaipur Commissionerate sold finished goods to its sister concern M/s Mangala Ispat (Jaipur) Limited, Jaipur on transaction value ₹ 74.11 crore, during December 2013 to March 2015. However, as per the provision of rule 8 ibid, value of goods works out to ₹ 78.00 crore. Thus the assessee suppressed the value of goods by ₹ 3.89 crore, on which duty payable, works out to ₹ 48.16 lakh, which was recoverable with interest.

Internal Audit was carried out by Department up to October 2014, partially covering the period, but it failed to detect the lapse.

When we pointed this out (November 2015), the Ministry admitted the observation (September 2016) and stated that the assessee deposited Excise duty of ₹ 48.16 lakh with interest of ₹ 10.62 lakh and penalty of ₹ 7.22 lakh. The assessee also agreed to pay differential duty from April 2015 onwards, as soon as CAS-4 certificate for the year 2015-16 would be prepared. On the lapse of Internal Audit, the Ministry stated that the explanation was being called for from the concerned audit officer.

(ii) Two units of M/s Pidilite Industries Ltd, (Registration nos. AAACP4156BXM002 and AAACP4156BXM011) in Raigad Commissionerate, are engaged in the manufacture of goods falling under Chapter 39 of the CETA, 1985. Scrutiny of sales invoices of 2014-15 revealed that the units had cleared excisable goods to its related units. However, no costing records to determine the cost of production had been maintained by them. The assessee was required to determine the cost of production as per CAS-4 and pay differential duty for the year 2014-15. This resulted in short payment of duty of ₹ 41.79 lakh, which was recoverable with interest.

The Internal Audit was conducted in June 2015 covering the period from February 2014 to March 2015, however, Audit Report was issued with 'Nil' objection.

When we pointed this out (August 2015), the Department stated that total duty of ₹ 41.79 lakh with interest of ₹ 7.73 lakh, was paid by both the units.

The Ministry contested the observation (November 2016) stating that the issue was periodical one and the assessee used to pay differential duty annually, in the month of October, for the previous year, after the availability of CAS-4 certificate. It also confirmed the payment of differential duty for the year 2014-15, amounting to ₹ 27.45 lakh, along with interest of ₹ 5.76 lakh, by one unit. On the lapse of Internal Audit, the Ministry stated that during the Internal Audit, the assessee stated that CAS-4 certificate was not ready and it was being finalized.

The reply of the Ministry is not tenable, as there is no provision to allow clearance of goods periodically without preparing CAS-4 certificate. In case, assessee was not able to decide the duty correctly, he should have opted for provision assessment under rule 7 of the Central Excise Rules, 2002. Also, if the assessee had not prepared the CAS-4 certificate during Internal Audit, the audit party should have raised the issue for monitoring of the same.

(iii) M/s BASF India Ltd in Belapur Commissionerate is engaged in the manufacture of excisable goods classifiable under Chapter 28 of CETA, 1985. Scrutiny of clearance details for the period 2012-13 and 2013-14, revealed that the assessee had cleared excisable goods amounting to ₹ 7.43 crore and ₹ 8.68 crore respectively to its related units. However, no costing records, to determine the cost of production, had been maintained by the assessee. The assessee was required to determine the cost of production as per CAS-4 and pay differential duty accordingly. Thus, non-adoption of correct assessable value on the clearances made to its related unit, resulted in sort payment of duty which was recoverable along with interest.

Though Internal Audit was carried out by the Department in December 2013, covering the period April 2010 to March 2013, the lapse remained undetected until pointed out by CERA.

When we pointed this out (April 2015), the Ministry admitted the observation (November 2016) and stated that the assessee had debited the differential duty of ₹ 87.36 lakh with interest of ₹ 29.39 lakh. On the lapse of Internal Audit, the Ministry stated that in the absence of CAS-4 certificate, the correct payment of duty could not be ascertained.

The reply of the Ministry is indicating that the Internal Audit failed to raise the issue for monitoring of the same.

(iv) M/s Tata Metaliks Ltd., Kharagpur in Haldia Commissionerate engaged in manufacture of Pig Iron, Molten Metal etc. cleared molted metal during the period 2013-14 to its related party M/s Tata Metaliks DI Pipes Ltd. (formerly M/s Tata Metaliks Kubota Pipes Ltd.), for further consumption by the related party, at a price lower than the one hundred and ten per cent of the cost of production. This was in violation of the aforementioned rule, resulting in short payment of excise duty of ₹ 18.34 lakh during the period 2013-14. The same was recoverable along with applicable interest.

Though Internal Audit of the unit was conducted in July 2014, the lapse remained undetected until pointed out by CERA.

When we pointed this out (April 2015), the Ministry admitted the observation (November 2016) and stated that the entire amount had been recovered with interest. On the lapse of Internal Audit, it stated that Internal audit was conducted in July 2014 for the period of 2013-14 and the financial documents i.e. balance sheet for the financial year 2013-14 were not finalized, therefore, lapse could not be detected.

The reply is not tenable as the objection could be detected from basic documents i.e. copy of CAS-4 certificate, prepared on monthly basis and invoices showing the clearance of molten metal.

(v) The audit of Office of the Superintendent of Central Excise, Annur-I Range, Tiruppur Division under Coimbatore Commissionerate was conducted during May and June 2014 where in the records of M/s Anugraha Valve Casting Limited, Unit-IV and M/s Jayachandran alloys (P) Ltd. were examined. Audit noticed that during the years 2012-13 and 2013-14, the assessees had cleared goods to their respective sister concerns for captive consumption by adopting rates which were less than one hundred and ten per cent of the cost of production of such goods, computed as per CAS-4 statement. The non-adoption of prescribed transaction value had resulted in under-valuation of goods and consequent short payment of duty, which has to be recovered along with applicable interest. Internal Audit conducted audit of the units in October 2013 and February 2014, but these aspects were not raised.

When we pointed this out (July 2014), the ministry admitted the observation (November 2016) and stated that M/s Anugraha Valve castings had paid duty of ₹ 7.09 lakh with interest of ₹ 4.03 lakh and M/s Jayachandran Alloys (P) Limited had paid duty of ₹ 3.47 lakh with interest of ₹ 0.65 lakh. On the lapse of Internal Audit, it stated that in case of M/s Jayachandran Alloys, explanations were being asked from the concerned officers. For M/s Anugraha Valve Castings, it stated that no Internal Audit was conducted

during 2012-13 to 2014-15 and information prior to this period was not available.

(Vi) M/s VVF (India) Limited, Kolkata falling under Kolkata-I Commissionerate (erstwhile Kolkata-V Commissionerate), engaged in manufacture of soap and toothpaste, transferred 4592.26 MT of manufactured soap noodles and neat soap to their sister units located at Baddi and Kutch during April 2011 to June 12, for captive consumption by those units. Hence, the assessee was liable to pay duty on 110 per cent of the cost of production, determined as per CAS-4 which was not done in this case and clearances were made on a lower assessable value. Subsequently, in November 2012, the assessee prepared a cost sheet and paid ₹ 64.13 lakh as differential duty and interest for above mentioned clearances but such cost sheet was not prepared in accordance with CAS-4 method and also did not include appropriate margin as required under rule. For discharging differential duty, assessable value in respect of soap noodles was determined by adding margin of five per cent only and in case of neat soap no margin was added to the cost of production. This resulted in short payment of duty of ₹ 10.31 lakh, which was recoverable along with applicable interest.

Internal Audit of the unit was conducted by the Department in March 2012. Provisions of Central Excise Audit Manual 2008, stipulates that audit should extend upto one completed month preceding the date of current audit. However, the lapse remained undetected until pointed out by CERA.

When we pointed this out (September 2013), the Ministry admitted the observation and stated (December 2016) that demand had been confirmed for ₹ 84.24 lakh along with applicable interest and penalty of ₹ 50.22 lakh. The assessee had paid ₹ 59.24 lakh with interest of ₹ 26.97 lakh. It further stated that issue was also detected by internal audit in November 2013.

The reply is not relevant to the audit observation which pointed out that the issue was not detected in the internal audit conducted in March 2012.

5.5.2.7 Short Payment of Duty Due to Incorrect Availing of Exemption

As per Notification 8/2003-CE dated 01 March 2003 as amended, the unit whose clearances was less than ₹ 4 crore in the previous year are entitled to full exemption up-to the clearance of ₹ 1.50 crore during the current Financial year in respect of specified goods listed in the annexure to the Notification. Further, as per para 2(i) of the said Notification, "a manufacturer has the option not to avail the exemption contained in this notification and instead pay the normal rate of duty on the goods cleared by him. Such option shall not be withdrawn during the remaining part of the financial year.' As per the said Notification, normal rate of duty means the aggregate of duty of

excise, specified in the First Schedule of the Central Excise Tariff Act, 1985 and the special duty of excise, specified in the Second Schedule of the Act, read with any relevant Notification issued under Section 5A(1) of the Central Excise Act, 1944. Notification No. 1/2011-CX dated 1 March 2011 was issued under Section 5A (1) of the Act.

M/s Intellectual Building Systems Private Ltd, in Pune-I Commissionerate, is engaged in the manufacture of precast hollow core slab, precast slab, ready mix concrete (RMC) etc. Scrutiny of ST-3 Return for the period 2011-12 to 2012-13 revealed that the assessee cleared RMC on payment of duty at the rate of 1 per cent and 2 per cent as applicable by availing Notification 01/2011-CE dated 01 March 2011 as amended, whereas for the clearance of other goods, the assessee availed value based exemption under Notification 08/2003-CE dated 01 March 2003 as amended and accordingly cleared such goods without payment of duty. Since the assessee had opted to clear RMC on payment of duty, the same should have been applicable for the clearances of all the other goods as stipulated in para 2(i) of the said notification. Non adherence to the above notification resulted in non-payment of duty amounting to ₹ 19.54 lakh which needs to be recovered alongwith interest.

Though Internal Audit was carried out by the Department in July 2013 covering the period September 2010 to June 2013, the lapse remained undetected until pointed out by Audit.

When we pointed this out (September 2014), the Ministry admitted the observation (November 2016) and stated that demand of ₹ 19.56 lakh was confirmed with interest and penalty of ₹ 9.78 lakh. On the lapse of Internal Audit, the Ministry stated that the assessee had not produced the required documents, though Departmental officer detected various other issues.

The reply is not acceptable as the assessee furnished details of exemption availed as per Notification No. 8/2003 and the duty paid on ready mix concrete in its ER-3 returns. Hence the issue should have been detected even during desk review. Detecting some issues can not be an excuse for leaving other lapses, involving recovery of revenue.

5.5.2.8 Short Payment of Duty due to Captive Consumption of Exempted Goods

Rule 4(1) of the Central Excise Rules, 2002 provides that every person who produces or manufactures any excisable goods, shall pay the duty leviable on such goods in the manner provided in Rule 8 and no excisable goods, on which duty is payable, shall be removed without payment of duty. Rule 2(K) of CENVAT Credit Rules, 2004 defines 'inputs' as all goods used in the factory by the manufacturer of the final products including accessories, all goods

used for generation of electricity or steam, for providing any output service but excludes goods used for (a) construction of execution of works contract of a building or a civil structure or a part thereof or (b) laying of foundation or making of structures for support of capital goods. Further, as per Sl. No. 206 of Notification No. 12/2012-CE dated 17 March 2012 (as amended) all goods falling under Chapter heading 7305 or 7308 are exempted from payment of duty, where goods are fabricated at site of construction work.

M/s Jindal Steel & Power ltd. Angul, under the jurisdiction of Bhubaneswar-II Commissionerate, engaged in manufacture of Calcined Lime, Steel Slab and Steel plate, used 3443.29 & 7225.78 MTs of fabricated steel structures viz. girder, Column, bracing etc. for its own consumption without payment of duty during 2013-14 and 2014-15 claiming exemption vide notification, ibid. The fabricated steel structures are falling under exclusion clause of the definition of inputs as they were consumed in structural work within the factory. Further, the assessee had claimed exemption under Notification ibid, which applies only in respect of goods fabricated at site of the work for use in construction work at such site. Therefore, the assessee was not entitled to exemption and as such duty of ₹ 5.45 crore was payable. Though Internal Audit was conducted, the lapse remained undetected until the issue was pointed out by Central Revenue Audit.

When we pointed this out (July 2015), the Ministry admitted the observation in principal (December 2016) but stated that issue was already in notice of the department and same was raised by Internal Audit in May 2015. It further stated that SCN for ₹ 6.26 crore was issued to the assessee and SCN for subsequent period was also under process.

The reply is not tenable as CERA Audit was conducted in April 2015 and Internal Audit raised the issue after being pointed out by CERA Audit.

5.5.3 Incorrect Availing of CENVAT Credit

5.5.3.1 Irregular Availing of CENVAT Credit on Ineligible Services

(i) Rule 2(l) of CENVAT credit Rules, 2004 as amended from time to time defines "Input Service" as any service "(i) used by a provider of taxable services for providing an output service, or (ii) used by the manufacturer, whether directly or indirectly, in or in relation to the manufacturer of final products and clearance of final products upto the place of removal; and includes services used in relation to modernization, renovation or repairs of factory premises of provider of output services 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, recruitments and quality

control, counseling and training, computer networking, credit rating, share registry and security, inward transportation of inputs or capital goods and outward transportation up to the place of removal".

M/s KEC International Ltd., Silvassa under Silvassa Commissionerate, availed CENVAT credit of Service Tax paid on Land Development, Housekeeping, gardening, grass cutting etc., during the period from 2009-10 to 2012-13 to the tune of ₹ 32.12 lakh. Since these services are not related to manufacturing activities, availing of CENVAT credit to the tune of ₹ 32.12 lakh was irregular and recoverable with interest.

Internal Audit of the Assessee was conducted in April 2012 for the period upto 2011-12 but failed to detect the lapse pointed out by CERA audit.

When we pointed this out (September 2013), the Ministry admitted the observation (September 2016) and stated that demand of ₹ 37.09 lakh along with interest and penalty had been confirmed. Assessee had appealed against the adjudication order. On the lapse of Internal Audit, the Ministry stated that the eligibility of disputed input service was subject to legal interpretations and different courts had decided that Garden Maintenance Service, Landscaping Service and Housekeeping Service were relating to manufacturer of final products. Hence, non-detection of such issue can not be considered as lapse of duty.

The reply of the Ministry appears contradictory as on one hand it has admitted the observation and on other hand it is stating that issues is subject to legal interpretation. Audit is of the view that Ministry need to issue suitable clarification to end the ambiguity on the issue of eligible services.

5.5.3.2 Irregular Availing of CENVAT Credit on Time Barred Invoices

According to Rule 4(1) of CENVAT Credit Rules, 2004, manufacturers or providers of output service is not eligible to take CENVAT credit on invoices, issued more than six months back. This provision was effective during the period from 1 September 2014 to 28 February 2015. Thereafter the six months barrier was changed to one year.

M/s Maithan Alloys Pvt. Ltd. in Bolpur Commissionerate took CENVAT credit of ₹ 76.07 lakh during September 2014 and November 2014 on invoices which were more than six months old. This resulted in irregular availing of CENVAT credit of ₹ 76.07 lakh and was recoverable along with applicable interest.

The assessee is a mandatory unit and the Internal Audit of the unit was conducted by the Department in May 2015 covering the period upto 2013-14, although the provisions of Central Excise Manual 2008, stipulates that

audit should extend upto one completed month preceding the date of current audit. The lapse remained undetected until pointed out by CERA.

When we pointed this out (September 2015), the Ministry while accepting the observation intimated (December 2016) credit reversal of ₹ 76.07 lakh by the assessee. Further, it stated that the auditors conducted the audit for the period as per the plan which was approved for 2013-14 and object raised by CERA pertains to 2014-15. It further added that the objection of CERA has been noted for future guidance.

The reply of the Ministry as regards to the non-coverage of the issue by the internal audit is not acceptable as Central Excise Manual 2008, stipulates that audit should extend upto one completed month preceding the date of current audit. As such the CERA's objection period i.e. 2014-15 should have been covered in internal audit in accordance with the laid provisions.

5.5.3.3 Irregular Availing of CENVAT Credit on Capital Goods, Exclusively Used for Manufacturing of Exempted Goods

As per rule 6 (4) of the CENVAT Credit Rules, 2004, capital goods used for manufacture of exempted goods or providing exempted service, are not eligible for CENVAT credit.

M/s Sangam (India) Ltd. in Udaipur Commissionerate engaged in manufacture of Polyster Viscose yarn, Cotton and Knitted yarn, availed CENVAT credit of ₹ 1.38 crore on imported machines, used exclusively in manufacture of exempted cotton yarn, during 2013-14. As machines were being used exclusively in the manufacturing of exempted goods, CENVAT credit amounting to ₹ 1.38 crore, availed on the same, was irregular.

Internal Audit was carried out by the Department for the period up to March 2014, partially covering the period mention in the audit observation but failed to detect the lapse.

When we pointed this out (March 2015), the Ministry admitted the observation (September 2016) and stated that SCN for ₹ 4.90 crore had been issued to the assessee. He had also deposited ₹ 50.00 lakh during investigation. On the lapse of Internal Audit, the Ministry stated that the explanation was being called for from the concerned audit officer.

5.5.3.4 Incorrect Availing of CENVAT Credit Pertaining to Other Unit

'Input service' is defined under Sub-Rule (l) of Rule 2 of the CENVAT Credit Rules, 2004 as any service used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products up to the place of removal. Interest is leviable under Rule 14

of the said Rules for belated reversal/repayment of wrongly availed CENVAT credit.

In Chennai-IV Commissionerate, it was noticed that unit-II of M/s. Dymos Lear Automotive India Private Ltd., Irungattukottai (Unit 2) had incorrectly availed (October 2010) input service tax of ₹ 17.89 lakh in respect of Intellectual Property service (paid under Reverse Charge basis) relating to another unit i.e. Unit-I . The incorrect availing of CENVAT credit was pointed out for reversal along with levy of interest applicable. Internal Audit conducted audit of the unit in March 2011, but this aspect was not raised.

When we pointed this out (March 2012), the Ministry admitted the observation (November 2016) and stated that the assessee had paid the duty of ₹ 17.89 lakh with interest of ₹ 14.93 lakh and penalty of ₹ 4.47 lakh. On the lapse of Internal Audit, the Ministry stated that reasons for the lapse were being ascertained from the audit team.

5.5.3.5 Incorrect Availing of CENVAT Credit of Duty Paid Under Suppression of Facts

Rule 9(1) (bb) of CENVAT Credit Rules (CCR), 2004 stipulates that CENVAT Credit shall be taken, based on a supplementary invoice, bill or challan issued by a provider of input service, in terms of provision of Service Tax Rules, 1994 except where the additional amount of tax became recoverable from the provider of service on account of any non-levy or non-payment or short payment by reason of fraud, collusion or any willful misstatement or suppression of acts or contravention of any provision of the Finance Act or the Rules made there under with intent to evade payment of Service Tax.

Head office (HO) at Mumbai (Input Service Distributor) of M/s. Welknown Polyesters Ltd, Daman (Unit–III) falling under jurisdiction of Daman Commissionerate, had obtained three loans (External Commercial Borrowings) from Germany and paid (2008-09 to 2010-11) certain charges (viz. up-front fees, management fee, commitment fee, security agent fees, appraisal fees etc.) to overseas service providers for obtaining these loans. Directorate General of Central Excise Intelligence, Ahmedabad issued SCN (January 2013) to the assessee's HO for non-payment of service tax on 'Banking and other financial services' from overseas service provider under the provisions of Section 66A of the Finance Act, 1994 of ₹ 105.44 lakh and suppression of facts after which the assessee paid total service tax of ₹ 30 lakh (vide challans dated 9 October 2012 and 20 March 2014) out of the total demand of ₹ 105.44 lakh issued to its HO. We noticed that the assessee availed CENVAT credit of the amount paid in November 2012 and March, 2014. Since the issue involved suppression of facts, CENVAT credit of

₹ 30 lakh was not admissible in terms of provision above. This resulted in incorrect availing of CENVAT credit of ₹ 30 lakh.

Internal Audit of the assessee was conducted by the Department in October 2014 for the period upto September 2014 but it failed to detect the observation raised by CERA audit.

When we pointed this out (August 2015) the Ministry admitted the observation (November 2016) and stated that SCN of ₹ 30.58 lakh was issued to the assessee. On the lapse of Internal Audit, it stated that incorrect credit was availed in the months of November 2012 and March 2014 and these months were not selected by Internal Audit, hence the lapse was not detected.

The reply is not tenable as the observation was based on SCN issued by DGCEI. The issue could have been detected even during desk review if the Assessee Master File had been prepared by Internal Audit by collecting information about SCNs issued for last three years.

5.5.3.6 Irregular Availing of Suo Moto Credit Against Refund

Notification 56/2003-CE dated 25 June 2003, as amended, provides area based exemption to specified goods cleared form state of Sikkim, by way of refund of duty that was paid through e-payment (PLA) after mandatory utilization of CENVAT credit available. According to the notification, the manufacturer in each month may take credit of amount paid and at the end of the financial year, differential amount if any shall be refunded by the Assistant Commissioner or the Deputy Commissioner of Central Excise by 15th day of May of subsequent financial year, subject to conditions as laid down. There is no scope of taking self credit of such differential amount by the manufacturer at his own.

M/s Sun Pharma Laboratories Ltd. and M/s Torrent Pharmaceuticals Ltd. Gangtok under Siliguri Commissionerate, after each financial year submitted refund claim of differential amount to the Department and availed self-credit of such differential amount in the subsequent months without having refund order issued by the competent authority. The refund claims of the assessees were neither scrutinized by the Department nor any refund order in respect of such claims were passed by the Department in stipulated time as was required under the statute. Availing credit of differential amount suo-moto and utilization of same for payment of Excise duty was irregular. This resulted in non-payment of duty of ₹ 5.39 crore during the period from 2010-11 to 2013-14, which was recoverable along with applicable interest.

M/s Sun Pharma Laboratories Ltd. was audited by Department in December 2013 while M/s Torrent Pharmaceuticals Ltd. was audited in February 2014.

However, the lapses in both the cases remained undetected until pointed out by CERA.

When we pointed this out (March 2015), the Ministry admitted the observation (November 2016) and stated that SCN for ₹ 4.06 crore had been issued to the assessee. On the lapse of Internal Audit, the Ministry stated that the assessee did not intimate the Range Superintendent regarding taking differential re-credit Suo-Moto. However, explanation had been called from the concerned officer.

The reply is not acceptable as the assessee intimated regarding availing of self credit of differential duty to the Deputy Commissioner of Gangtok Division with a copy to the Superintendent of the Gangtok Range. Hence, Department was aware about the fact of availing self credit.

5.5.4 Non/Short Reversal of CENVAT Credit

5.5.4.1 Non-Reversal of CENVAT Credit on Obsolete Input

Rule 3(5B) of CENVAT Credit Rules 2004 provides that if the value of any input or capital goods, before being put to use, on which CENVAT credit has been taken is, written off fully or partially or where any provision to write of fully or partially has been made in the books of account, then the manufacturer or service provider, as the case may be, shall pay an amount equivalent to the CENVAT credit taken in respect of the said input or capital goods.

(i) M/s Hindustan Zinc Ltd. (HZL), Chanderiya in Udaipur Commissionerate, had made provisions of non-moving inventory of store items/inputs valuing ₹ 11.71 crore during 2012-13 to 2013-14 in their books of accounts. Since these provisions were made before store items/inputs being put to use, the assessee was required to pay an amount of ₹ 1.69 crore as per provision of rule ibid, which was not paid.

Internal Audit, though carried out up to March 2013, partially covering the period mentioned in the LDP, had not pointed out the lapse deducted by CERA.

When we pointed this out (January 2015), the Ministry admitted the observation (November 2016) and stated that SCN for ₹ 17.22 crore had been issued to the assessee. On the lapse of Internal Audit, the Ministry stated that the explanation was being called for from the concerned audit officer.

(ii) M/s National Engineering Industries Limited in Jaipur Commissionerate had made provision of ₹ 1.53 crore in the books of account towards obsolete inputs during 2013-14 and 2014-15. However, CENVAT credit attributable to these inputs, amounting to ₹ 18.96 lakh, was not paid which was recoverable with interest.

Internal Audit of the assessee was carried out by the Department but it failed to detect the lapse pointed out by Audit.

When we pointed this out (January 2016), the Ministry admitted the observation (November 2016) and stated that the assessee had debited the amount and deposited ₹ 18.96 lakh with interest of ₹ 7.68 lakh and penalty of ₹ 2.84 lakh. On the lapse of Internal Audit, the Ministry stated that Internal Audit is selective audit, based on approved audit plan where no point related to CENVAT credit on obsolete input was specifically mentioned.

The reply is not tenable as provision of obsolete input/capital goods are mentioned in annual financial statement and detailed examination of these statements is to be compulsorily done by the Audit.

5.5.4.2 Non-Reversal of CENVAT Credit on Exempted Clearances

Rule 6(1) of CENVAT Credit Rules, 2004, envisages that CENVAT credit shall not be allowed on such quantity of input or input service which is used in the manufacture of exempted goods or for provision of exempted services. In case the manufacturer opts not to maintain separate accounts of inputs used for manufacture of taxable and exempted goods, then as per rule 6(3), the manufacturer shall follow any one of the following options, as applicable to him, namely:-

(i) Shall pay an amount equal to six per cent of value of the exempted goods; or

(ii) Shall pay an amount equivalent to the CENVAT credit attributable to inputs and input services used in or in relation to manufacture of exempted goods as determined under sub-rule 6(3A); or

(iii) Maintain separate accounts of inputs and take CENVAT credit only on inputs used for manufacture dutiable final products and pay an amount equivalent to the CENVAT credit attributable to input services used in or in relation to, the manufacture of exempted goods as determined under sub-rule 6(3A).

Further, as per rule 6(2) of CCR, 2004 maintenance of separate accounts for 'inputs' entails keeping of separate account for receipts, consumption and inventory of inputs used in or in relation to manufacture of dutiable and exempted goods and taking CENVAT credit only on 'inputs' used in dutiable goods.

Verification of records at M/s Sun Pharma Laboratories Ltd. Gangtok in Siliguri Commissionerate revealed that the assessee manufactured and cleared both dutiable and exempted Pharmaceutical products and opted to maintain separate accounts for inputs as provided in the rule 6(3) (iii) of CCR

2004. Audit scrutiny, however, revealed that the assessee adopted a system of taking and utilizing entire credit on inputs received in the factory for manufacture of dutiable and exempted products. Subsequently, before the manufacture of exempted goods, the assessee reversed the CENVAT credit attributable to exempted goods being manufactured. Thus, the assessee failed to maintain separate account for inputs as stipulated in rule 6(3)(iii) and 6(2) of CCR 2004 and ought to have paid six per cent of value of the exempted goods. This resulted in short payment of ₹ 9.34 crore during 2012-13 and 2013-14 which is recoverable with interest.

The assessee is a mandatory unit and is required to be covered annually in Internal Audit as per Department norms. The said unit was last audited in December 2013 covering the period 2012-13. But the lapse remained undetected until pointed out by CERA.

When we pointed this out (March 2015), the Ministry contested the observation and stated (December 2016) that the assessee has option either to maintain separate account or pay an amount equivalent to the CENVAT credit attributable to inputs used in exempted goods. In this case the assessee reversed the proportionate credit.

The reply is not acceptable, as the rule require assessee to intimate the department about the option exercised and follow the same which is not adhered to in this case.

5.5.4.3 Non-Reversal of Proportionate CENVAT Credit on Services Used in Trading

As per Rule 6(3) of CENVAT Credit Rules 2004, the manufacturer of goods or provider of services, opting not to maintain separate accounts for receipt and use of inputs/input services in the manufacture of both dutiable and exempted goods or provision of taxable and exempted services has got the option of paying an amount under Rule 6(3)(i) at the prescribed percentage on the value of the exempted services/exempted goods or paying an amount determined by the method prescribed under Rule 6(3A). Trading is an 'exempted service' as per the explanation under Rule 2(e) of the said rules.

M/s Spraying Systems India Pvt. Ltd., Bangalore under Bengaluru-II Commissionerate, was using its registered premises for trading of various goods in addition to manufacture of excisable goods. The assessee availed CENVAT credit of Service Tax paid on rent of factory building, charges for security services, Chartered Accountant's services, etc., the services of which were commonly utilised for manufacturing and trading activities. Since the assessee did not maintain separate accounts in respect of utilization of these input services for manufacturing of duty paid goods and for providing

exempted services (trading), the assessee should have paid 5/6 per cent of value of exempted service or amount to CENVAT credit involved in exempted service.

Internal Audit was conducted twice, covering the period upto August 2013, but it failed to detect the lapse.

When we pointed this out (June 2014), the Ministry stated (September 2016) demand of ₹ 47.41 lakh was confirmed and the assessee paid ₹ 18.94 lakh.

For the lapse of Internal Audit, the Ministry stated that Internal Audit was conducted by the Department in 2012 and 2015 and the issue was long before detected by it and recovery of ₹ 18.94 lakh had been made.

The reply of the Ministry is not tenable as assessee was audited twice before CERA audit but the issue was not detected by them as evident from Audit note Nos. 248/2012 dated 28 August 2012 and 380/2013 dated 4 December 2013. Then, CERA conducted the audit of the assessee in April-May 2014 and raised the issue in June 2014. Subsequently, the third audit was conducted by the Department in October 2014, which detected the issue and audit note No. 469/2014 was issued containing an observation on the issue and stating that ₹ 4.89 lakh was recovered. Thus, Ministry's statement that issue was long before detected by Internal Audit, is not correct.

Thus, Internal Audit not only failed to detect the lapse of the assessee, it also tried to give wrong facts to hide its lapse. Ministry may examine the facts and suitable action may be taken against the erring officials.

5.5.4.4 Non Reversal of CENVAT Credit on Electricity and Security Trading

As per Rule 6 of the CENVAT Credit Rules, 2004 (CCR), CENVAT credit shall not be allowed on such quantity of input or input service which is used in the manufacture of exempted goods or for provision of exempted services. The term 'exempted services' as defined in rule 2 (e) means taxable services which are exempt from the whole of the Service Tax leviable thereon and also include services on which no Service Tax is leviable under section 66B of the Finance Act, 1994. As per Rule 6(2) of CCR, where a manufacture or provider of output service avails inputs and input services and manufacture dutiable as well as exempted goods or provides taxable as well as exempted services, separate accounts shall be maintained for the receipt, consumption and inventory of inputs used and receipt and use of input services used in or in relation to the manufacture of dutiable and exempted goods and for the provision of taxable and exempted services. If the separate accounts as mentioned above are not maintained, the manufacturer or service provider shall pay an amount as per provisions contained Rule 6(3) of CCR, 2004. Further the difference between the sale price and the purchase price of the

securities traded or one per cent of the purchase price of the securities traded, whichever is more, shall be treated as the value of exempted services as per notification 28/2012(CX) in case of trading of securities.

M/s Godrej Industries Ltd. in Mumbai-II Commissionerate is engaged in the manufacturer of excisable goods falling under chapter heading 34, 38 and 39 of CETA 1985. Scrutiny of financial statements of 2012-13 revealed that the assessee had carried out trading activity of ₹ 13.83 crore at their retail shop and also sold electricity generated form windmill amounting to ₹ 4.26 crore. It was also observed that during the same year assessee had earned profit on sale of investment of ₹ 74.77 lakh. However, assessee neither maintained separate account nor paid any amount under rule 6(3) of the CENVAT Credit Rules, 2004 as per above provision. This resulted in non-reversal of CENVAT credit to the tune of ₹ 14.59 crore.

Internal Audit, though carried out up to March 2013, had not pointed out the lapse detected by CERA.

When we pointed this out (March 2014), the Ministry admitted the observation (November 2016) and stated that SCN for ₹ 14.59 crore had been issued to the assessee. On the lapse of Internal Audit, the Ministry stated that the explanation was being called for from the concerned audit officer.

5.5.4.5 Non-Reversal of CENVAT Credit on Input Value Set Off by Credit Notes

Rule 14 of the CENVAT Credit Rules, 2004 stipulates that where CENVAT credit has been taken and utilized wrongly, the same shall be recovered from the manufacturer and the provisions of section 11A shall apply for effecting such recoveries.

During the audit of the Office of the Superintendent of Central Excise, Irungattukottai-III Range, Sriperumpudur Division falling under Chennai-IV Commissionerate, the accounts of an assessee, M/s Surin Automotive Pvt. Ltd. was taken up for detailed scrutiny. On a scrutiny of the CENVAT records maintained for the years 2012-13 and 2013-14, it was noticed that the assessee had received imported/ indigenous raw materials from their supplier, M/s Sungwoo Gestamp Hitech (Chennai) Ltd. and availed CENVAT credit passed on provisionally by the supplier without taking into account the credit notes issued by the supplier at the end of each month. This resulted in excess availing and utilization of CENVAT credit amounting to ₹ 14.72 lakh for the year 2012-13 and ₹ 27.93 lakh for the year 2013-14. Internal Audit conducted audit of the unit in December 2014, but this issue was not raised.

When we pointed this out (December 2015), the Ministry admitted the observation (November 2016) and stated SCN for ₹ 40.62 lakh had been

issued to the assessee. On the lapse of Internal Audit, the Ministry stated that Commissioner (Audit II) had been asked to take action against the audit officer who failed to detect the lapse.

5.5.4.6 Short Reversal of CENVAT Credit on Inputs Cleared as Such

As per Rule 3(5) of the CENVAT Credit Rules 2004, when inputs or capital goods on which CENVAT credit has been taken, are removed as such from the factory or premises of the provider of output service, the manufacturer of the final product or the provider of output service as the case may be, shall pay an amount equal to the credit availed in respect of such inputs or capital goods. Further, as per rule-14 of the Rules, ibid, when CENVAT credit has been taken and utilised wrongly or has been erroneously refunded, the same along with interest shall be recovered from the manufacturer or the provider of output service.

Audit of ER-1, Sales Register, CENVAT credit Register of M/s HINDALCO Industries Ltd. (Flat Rolled Product Unit) Hirakund, for the year 2013-14, a manufacturer of Aluminium Flat rolled Products (Ch. 76069290) under the jurisdiction of Rourkela Commissionerate, revealed that the assessee had availed CENVAT credit of ₹ 1.90 crore on inputs i.e. CG Ingots. However, the same were removed as such on payment of duty of ₹ 1.52 crore, resulting in short reversal of CENVAT credit of ₹ 37.61 lakh, in contravention to the Rule, ibid.

When we pointed this out (August 2015), the Ministry admitted the observation (November 2016) and stated that the assessee had reversed amount of ₹ 37.61 lakh along with interest of ₹ 10.53 lakh. On the lapse of internal Audit, it stated that Internal Audit was conducted on test check basis and the issue escaped the attention of Internal Audit.

5.5.4.7 Short Reversal of CENVAT Credit Availed on Inputs Destroyed in Fire

Rule 21 of Central Excise Rules, 2002 provides that where it is shown to the satisfaction of the Commissioner that goods have been lost or destroyed by natural causes or by unavoidable accident or are claimed by the manufacturer as unfit for consumption or for marketing, at any time before removal, he may remit the duty payable on such goods, subject to such conditions as may be imposed by him by order in writing. Rule 3(5C) of the CENVAT Credit Rules, 2004 further provide that where on any goods manufactured or produced by an assessee, the payment of duty is ordered to be remitted under Rule 21 of the Central Excise Rules, 2002, the CENVAT credit taken on the inputs used in the manufacture or production of said goods shall be reversed.

Test check of records of M/s Akal Electricals Pvt. Ltd. Doraha, engaged in the manufacturing or transformers under chapter 8504, in Ludhiana Commissionerate revealed that inputs (Transformer Oil, CRGO, Aluminium, Copper) which were destroyed in a fire incident in August 2008, were written off by the assessee during 2008-09 and CENVAT credit of ₹ 33.38 lakh was reversed. However, amount of CENVAT credit to be reversed worked out to ₹ 76.09 lakh. This resulted in short reversal of CENVAT credit amounting to ₹ 42.71 lakh.

Internal Audit, though carried out in May 2010, covering the period mentioned in audit observation, failed to detect the lapse.

When we pointed this out (April 2010), the Ministry admitted the observation (November 2016) and stated that that the SCN issued to the assessee had been adjudicated, confirming the demand of ₹ 76.09 lakh alongwith equal penalty and interest. Assessee filed appeal before CESTAT which was pending. On the lapse of Internal Audit, it stated that the issue was examined by Internal Audit but the assessee had not provided claim filed with insurance company at the time of Audit.

5.5.4.8 Short Reversal of CENVAT Credit on Used Capital Goods

Rule 3(5A) of CENVAT Credit Rules, 2004 provides for the procedure on removal of used capital goods, wherein an assessee needs to pay an amount equal to credit availed after allowing depreciation at the rate of 2.5 per cent per quarter subject to the condition that if the amount computed is less than the duty payable on 'Transaction Value', then amount equal to duty on 'Transaction Value' has to be paid.

M/s Bothra Shipping Services Pvt. Ltd. under Visakhapatnam-I Commissionerate, had sold used capital goods for a transaction value of ₹ 1.94 crore for which duty of ₹ 23.98 lakh was payable as per the rule ibid. However, the assessee reversed CENVAT credit of ₹ 16.14 lakh only after availing depreciation of 2.5 per cent per quarter. This resulted in short reversal of CENVAT credit of ₹ 7.84 lakh which was recoverable with interest of ₹ 3.60 lakh. Similarly M/s HBL Power Systems Ltd. sold capital goods for ₹ 98.08 lakh on which duty of ₹ 12.12 lakh was payable but the assessee paid ₹ 8.54 lakh. This resulting in short payment of credit of ₹ 3.59 lakh which was recoverable with interest of ₹ 2.12 lakh. The short reversal of CENVAT credit and interest payable aggregated to ₹ 17.15 lakh was recoverable.

Though, Internal Audits of the two assessees were conducted upto September 2014 and January 2015, the short reversal was not noticed.

When we pointed this out (January-February 2016), the Ministry admitted the observation (December 2016) and stated that M/s Bothra Shipping

Services Pvt. Ltd. reversed the duty of ₹ 7.84 lakh along with interest of ₹ 3.60 lakh and M/s HBL Power Systems Pvt. Ltd. reversed the duty of ₹ 3.59 lakh along with interest of ₹ 2.12 lakh. On the lapse of Internal Audit, it stated that in Internal Audit, CENVAT issues were randomly verified for sample months and the months examined by CERA Audit were not covered in sample.

5.5.4.9 Short-Reversal of CENVAT Credit on Common Input and Input Services

As per Rule 6(3)(ii) of CENVAT Credit Rules, 2004, the manufacturer of goods or the provider of output service, opting not to maintain separate accounts for receipt and use of inputs/services in the manufacture of both dutiable and exempted goods, has got the option of paying an amount determined by the formula prescribed under Rule 6(3A).

M/s Pepsico (I) Holdings Pvt. Ltd., Bangalore, under Bangalore – III Commissionerate, a manufacturer of carbonated soft drinks, mineral water, fruit juice and syrups had cleared fruit juice by availing the benefits of exemption under Notification No.1/2011-CE dated 01 March 2011 during 2011-12, in addition to clearance of other final products on payment of duty. The assessee availed CENVAT credit on inputs and input services utilised commonly for manufacture of the dutiable and the exempted final products, but did not maintain separate accounts in respect of them. The assessee reversed a portion of the CENVAT credit as per the provisions of Rule 6(3A) amounting to ₹ 27.25 lakh against ₹ 1.24 crore, reversible during the year 2011-12, resulting in short reversal of ₹ 96.71 lakh which was recoverable with interest.

Though the Internal Audit (December 2012 to January 2013) was conducted covering the period 2011-12, it failed to detect the short reversal.

When we pointed this out (December 2014), the Ministry stated (September 2016) that SCN for ₹ 96.47 lakh had been issued to the assessee and assessee had filed an appeal before the CESTAT. On the lapse of Internal Audit, the Ministry stated that the Department only verified documents for a particular test month as per the pre-approved audit plan and if the issue was non-existent during the said test checked month, the issue could not have been detected.

The reply of the Ministry is not tenable as CERA noticed short reversal of CENVAT credit in all the months of the year 2011-12 which was included in the period of 22 months (January 2011 to October 2012) covered by Internal Audit.

Thus, Internal Audit not only failed to detect the lapse of the assessee, it also tried to give wrong facts to hide its lapse. Ministry may examine the facts and suitable action may be taken against the erring officials.

5.5.5 Non-Payment of Interest

5.5.5.1 Non-Payment of Interest on Payment of Differential Duty

Section 11AA of the Central Excise Act, 1944, envisages that where any duty of excise has not been levied, the person, in addition to the duty, is liable to pay interest at the rate specified after due date in which the duty ought to have been paid.

M/s BESCO Ltd. (Unit-I) and M/s Gontermann-Peipers (India) Ltd. in Kolkata-V Commissionerate, M/s Hindustan Unilever Ltd. in Haldia Commissionerate paid differential duty at a later date for collection of extra amount in respect of sales made earlier. The assessee however failed to pay interest on such delayed payment of duty. Non-payment of interest in respect of M/s BESCO Ltd. was ₹ 4.70 lakh for the period 2013-14 and 2014-15, in respect of M/s Gonternmann-Peipers (India) Ltd. such interest amount was ₹ 8.53 lakh for the period 2013-14 and in respect of M/s Hindustan Unilever Ltd. the same was ₹ 4.98 lakh for the period 2013-14 and 2014-15.

M/s BESCO Ltd (Unit-I) was audited by the Department in January 2013 covering the period 2011-12, although, as per the audit manual the same should have been covered upto December 2012. M/s Gontermann-Peipers (India) Ltd. was taken up for Internal Audit by the Department in June 2015 covering the period 2013-14 only. M/s Hindustan Unilever Ltd., although, was a mandatory unit and was required to be covered annually in Internal Audit as per Departmental norms but the unit was not audited since July 2013. In all the three cases the lapse remained undetected until pointed out by us.

When we pointed this out (Between March 2015 and September 2015), the Ministry contested the observation (October 2016) stating that Supreme Court in the case of M/s SAIL [2015(326) ELT 450] viewed that interest was not payable in case of payment of differential duty. The matter has been transferred to larger bench and judgment is pending. It further stated that as the objection is contested, the lapse on part of Internal Audit does not arise.

The reply is not tenable, as in the case of sub-judice issue, objection should have been raised and SCNs should have been transferred to call book, so that, if the issue is decided in favor of the Department, there is no revenue loss. In the absence of issuance of demand, the issue will be time barred even if matter is decided in favor of the Department. Ministry need to examine the issue and issue suitable instruction to field formations.

5.6 Miscellaneous Issues

5.6.1 Incorrect Reduction of Penalty and Non-Detection of Short Payment of Interest

According to first proviso to section 11 AC of Central Excise Act 1944, where any duty, as determined under sub-section 2 of section 11A and the interest payable thereon under section 11 AB, is paid within thirty days of the date of communication of order of the Central Excise Officer, who has determined such duty, the amount of penalty liable to be paid by such person shall be twenty five per cent, of the duty so determined.

M/s Gasha Steels Pvt. Ltd. Kanjikode, under Calicut Commissionerate was engaged in clandestine removal of CTD/TMT bars and scrap, on parallel invoices during the period May 2004 to February 2006. Duty payable on this removal amounted to ₹ 67.77 lakh and interest was also payable. SCN, demanding duty of ₹ 67.77 lakh alongwith interest and penalty, issued, based on an offence case, was confirmed vide Order in Original (O-I-O), dated 12 May 2009 alongwith interest and penalty of ₹ 67.77 lakh. Personal penalty of ₹ 20,000 each was also imposed on Director and Managing Director (MD).

As per the O-I-O, if the duty and interest under section 11 AB of the Act was paid within thirty days of receipt of the order, the amount of penalty shall be restricted to 25 per cent of the amount of duty confirmed. It was also ordered to adjust ₹ 30.00 lakh and ₹ 20.00 lakh already paid by the assessee in February 2006 and June 2006 respectively, towards demand of duty confirmed. The assessee paid (July 2009) balance duty of ₹ 17.78 lakh, penalty of ₹ 16.94 lakh, being 25 per cent of duty confirmed and interest. The assessee, however, paid interest of only ₹ 0.19 lakh as against interest of ₹ 12.27 lakh, payable for the period May 2004 to July 2009. The assessee also preferred appeal in CESTAT misrepresenting that the full amount of duty alongwith interest and penalty have been deposited and also informed (July 2009) jurisdictional Superintendent accordingly. Department, however, overlooked the misrepresentation made by the assessee regarding non-payment of interest in full. This had resulted in short payment of interest of ₹ 12.08 lakh. Further, the assessee was also not entitled for the benefit of reduced penalty of 25 per cent as they failed to discharge the interest liability in full. Even though Internal Audit of the assessee covering the period upto June 2011 was conducted in July 2011, this lapse was not found out.

When this was pointed out (December 2011), the Department replied (August 2012) that no coercive action was taken to realize the dues since two stay orders against recovery of penalties were issued (January 2010 and February 2010) by CESTAT.

CERA pointed out (October 2012) that the stay orders were only in relation to personal penalty imposed on the MD and Director and that while granting these stays, the Tribunal observed that the entire amount of duty, Interest and penalty confirmed was deposited by the main appellant. Clarification was also sought from the Department regarding informing CESTAT about the short payment of interest by the party and consequent ineligibility for reduced penalty.

The Department stated (April 2014) that a Miscellaneous Application was filed (January 2014) in CESTAT submitting that the assessee was yet to pay the interest of ₹ 12.08 lakh and balance penalty of ₹ 50.83 lakh and that the assessee have misrepresented facts before the Tribunal. The Department also informed (December 2014) about initiation of action under section 11(2)(i) of the Act for recovery of balance interest of ₹ 12.08 lakh and penalty of ₹ 50.83 lakh. The CESTAT rejected (March 2014) the miscellaneous application stating that it was filed not in respect of appeal filed by M/s Gasha Steels, against O-I-O 11/2009 CE dated 12 May 2009, but in respect of stay orders granted to the MD and a Director for waiver of pre-deposit and against recovery of personal penalty. The Tribunal also cited delay of nearly four years in filing the miscellaneous application and stated that there was no stay against recovery of entire amount of interest and balance penalty and the Department could have recovered the same from the assessee/ appellant M/s Gasha Steels.

The Department further stated (July 2015 and November 2015) that the assessee had filed (June 2015) writ petition along with stay application in Hon. High Court of Kerala to quash the O-I-O and to restrain recovery of balance amount of interest and penalty.

The Department was under the impression that the assessee had paid the entire amount of interest so they were eligible for reduced penalty of 25 per cent and that CESTAT stayed recovery of interest and penalty. This revealed absence of a system in place for proper monitoring and follow up of recovery of un-stayed confirmed demands. Lapse on the part of Department in understanding the facts of the case and ascertaining that the stay orders were only in respect of personal penalty against the MD and a Director had resulted in non-initiation of action in a case where there was no stay for recovery of arrears in respect of interest amounting to ₹ 12.08 lakh and balance penalty of ₹ 50.83 lakh (75 per cent) of nearly seven years. This had also resulted in extension of unwarranted financial accommodation to the assessee since no interest was leviable on arrears of interest amount relating to the period May 2004 to July 2009 and as no action was taken for recovery of un-stayed interest and penalty for nearly seven years.

Ministry stated (December 2016) that CERA's observation 'reduction of penalty was granted to the assessee' was not correct as the Department intimated CESTAT (January 2014) that the assessee was yet to discharge the interest liability of 12.08 lakh and was not entitled for the reduced penalty of 25 *per cent*.

The reply is not tenable as the Department intimated CESTAT about non-payment of interest only after clarification for the same was sought by CERA from the department.

5.6.2 Raising of Short Demand in SCN

Under the provisions of section 11A and 11AA of the Excise Act, Central Excise Officers are empowered to serve a notice, within the period of limitations prescribed, requiring a person chargeable with duty which has been short paid to show cause as to why he should not pay the short paid duty specified in the SCN.

Audit of the Central Excise receipts and refunds relating to the Office of the Assistant Commissioner of Central Excise, LTG III Group under LTU Commissionerate was conducted from June 2015 to September 2015 wherein Audit noticed from two SCNs issued to M/s. CPCL, Manali, Chennai for the years 2012-13 and 2013-14 that the differential duty payable by the assessee on account of reversal of CENVAT on exempted goods, was erroneously specified therein, resulting in short raising of demand amounting to ₹ 14.53 lakh and ₹ 62.02 lakh respectively. This was due to non-verification of assessees claim by the Department resulted in short raising of demand.

When we pointed this out (October, December 2015), the Ministry accepted the observation and stated (December 2016) that differential duty was payable, though, there was no error in the SCNs regarding the gross demands. It was further stated that shortcomings in the system of issue of SCNs has been noted and necessary action are being initiated.

The reply is not acceptable as the issue was not about the gross demands but about the determination of net amount payable after incorrectly adopting the amount already reversed which have since been paid by the assessee.

5.6.3 Irregular Transfer of SCN to Call Book

CBEC Circular No. 162/73/95-CX dated 14 December 1995, specifies the circumstances under which a case can be transferred to Call Book as below:-

(i) Cases in which the Department had gone in appeal to the appropriate authority,

(ii) Cases were injunction had been issued by Supreme Court/ High Court/ CEGAT. Etc.

(iii) Cases where audit objections were contested,

(iv) Cases where the Board had specifically ordered the same to be kept pending and to be entered into the Call Book.

Also, instructions were being issued to the Commissionerates requiring periodical review of pending Call Book items.

Scrutiny of SCNs pending in Call Books (May 2015) at the Office of the Commissioner of Central Excise, Bangalore-III Commissionerate, revealed that the SCN dated 01 February 2011 issued to M/s Victoria Marine and Agro Exports Ltd. Bangalore, demanding ₹ 3.70 crore towards CENVAT credit availed/ utilised irregularly, was pending for adjudication. However, the SCN was transferred (April/May 2012) to Call Book with the remarks that "further verification required" although the case did not fit into any of the categories mentioned above. Even after the Department noticed (January 2014), during subsequent review of Call Book cases, that the case was not fit for retention in Call Book, the same was not taken out of Call Book for adjudication.

When we pointed this out (May 2015), the Ministry stated (October 2016) that SCN had been taken out from call book and adjudicated in December 2015, resulting in confirmation of demand of ₹ 3.70 crore and penalty of ₹ 5.14 crore. The Ministry further stated that issue was already detected by the Department in review of call book and was same was inadvertently remained in call book.

Though, the wrong retaining of SCN in call book was detected by the Department, no remedial action was taken, till the same was pointed out by CERA and case was adjudicated in December 2015. Had the Department taken timely action, demand of ₹ 8.84 crore could have been decided earlier. Ministry need to look into the matter and take necessary action against the erring official as deemed fit and take effective steps to avoid similar lapses in future.

5.6.4 Avoidable Expenditure on Payment Towards Electric Power Consumption

The office complex of Commissionerate of Central Excise, Belagavi, is maintained by Central Public Works Department (CPWD). The Commissionerate entered into a contract with Karnataka Electricity Board [presently, Hubli Electricity Supply Company Ltd. (HESCOM)], Belagavi for supply of 210 KVA (contract demand) power. As per the agreement, the Commissionerate has to pay 75 per cent of the contract demand of 210 KVA

i.e., 158 KVA (demand contract) or the actual usage (recorded demand) whichever is higher.

A review of electricity supply bills and the allied records conducted during the audit of Belagavi Commissionerate for the period 2007-08 to 2014-15 revealed that, the Commissionerate paid electricity charges for 158 KVA per month as the recorded demand ranged only between 38.42 KVA and 68.94 KVA per month, during the said period. Thus, the actual power demand varied between 18 to 33 per cent of the contract demand. No action was taken by the Commissionerate to reduce the contract demand to an acceptable level of 100 KVA. Failure to take timely action to reduce the contract demand, resulted in incurring excess expenditure of ₹ 15.13 lakh during the period from 2007-08 to 2014-15, which was avoidable.

When we pointed this out (April 2013), the Department replied (July 2016) that HESCOM reduced (June 2016) the contract demand to 100 KVA per month. The Ministry stated (November 2016) that it was a technical issue requiring technical opinion of executive (Electrical) CPWD Bangalore. The electricity requirement, planning designing etc was done by CPWD and the demand of 210 KVA was arrived at by them at the time of construction of the building. The issue was not known to the Department and all the aspects, electricity requirement, demand and supply were being handled by the CPWD.

The reply is not tenable as electricity supply was being handled by CPWD but the electricity bills were being received and payments were being made by the Commissionerate. Since, the electricity consumption by the office was less than the contracted demand, it should have take action to reduce the demand. The Department even took more than three years to take action, after issue been pointed out by CERA which resulted in continuity of the avoidable expenditure.

5.6.5 Irregular Payment of Tribal Area Allowance

As per the Government of India, Ministry of Finance order (August 2008), the concession of Scheduled Area/ Tribal Area Allowance (TAA) to the Central Government employees is of temporary nature and will be reviewed by the Government at appropriate time in the light of the continued admissibility or otherwise, of the allowance to the State Government employees in the respective areas. Besides, TAA shall ceases to be admissible in those States where it has been discontinued for the State Government employees. Further, Government of India, Ministry of Finance, Department of Revenue, New Delhi vide Office Memorandum No. 17(1)/2008-E.II(B) dated 22 March