CHAPTER III
UTILISATION OF CENVAT CREDIT

In this chapter, we have reported cases where assessees paid duty (utilised) from their accumulated credit in contravention of rules which resulted in revenue loss of ₹ 257.31 crore.

3.1 Transfer of unutilised credit

By insertion of sub-section (1A) under section 5A of the Central Excise Act, 1944, with effect from 13 May 2005, it has been made obligatory on the manufacturer not to pay duty on exempted goods. The Board had also clarified on 4 January 1991 (Circular No. 02/91-CX3) that an assessee has no option to pay duty on his own volition in case of goods which are fully exempt from payment of duty.

It follows from the provisions that if any amount is paid as excise duty which is not leviable by law, it would be in the nature of deposit with the Government and therefore, availing of credit of such extra duty paid is not correct. We found that 21 manufacturing units in nine commissionerates, had passed on unutilised credit of ₹ 143.46 crore to its sister concerns or downstream manufacturers between April 2003 and March 2008 by overpaying duty through different methods such as payment of duty at higher rate than the actual effective rate of duty; payment of duty on exempted goods or goods chargeable to nil rate of duty; payment of duty at higher value etc. An assessee who is unable to utilise his cenvat credit fully can use this modus operandi to derive benefit by transferring credit to a downstream unit. He gets cash (the duty component received from the downstream unit) against his accumulated cenvat credit which might not have been utilised for a long time. In other words, it is a way of encashing his accumulated credit. The department had admitted observations in two cases involving credit of ₹ 8.36 lakh and reported recovery of ₹ 9.14 lakh (including interest). Reply in the remaining cases had not been received (December 2010).

Two such cases are illustrated below:

3.1.1 M/s Jindal Stainless Ltd., and M/s Vedanta Aluminium Ltd., in Bhubaneshwar-I commissionerate and M/s HINDALCO Industries Ltd., in Bhubaneshwar-II commissionerate, engaged in the manufacture of high carbon ferro chrome, calcined alumina etc. cleared a major portion of their finished goods to their sister units for further use in the manufacture and the rest was cleared for export. A small quantity of finished goods was cleared to customers as direct sale. Since major portion of finished goods was cleared to sister units and for export, it had little scope to utilise the accumulated cenvat credit. The assessee paid duty on goods transferred to the sister units much above the applicable value (110 per cent of cost). It succeeded in passing on cenvat credit to the tune of ₹ 58.76 crore during the years from 2005-06 to

2007-08. The payment of duty in excess of the duty payable was deposits and therefore, availing of credit by sister unit was not correct.

When we pointed this out (April 2008, February and March 2009), the department intimated (October 2009) that in the case of M/s Jindal Stainless Ltd. and M/s Vedanta Aluminium Ltd., there was no revenue loss. In the case of M/s. HINDALCO Industries Ltd., the department stated (September 2010) that there was no provision in the Cenvat Credit Rules, to reverse the credit for overvaluation of finished goods.

The reply of the department was not in consonance with section 5A (1A) and the Board's clarification of 4 January 1991. Moreover, as already pointed out, this was being used to encash accumulated cenvat credit.

3.1.2 M/s Jayaswal Neco Industries Ltd., M/s Jindal Steel & Power Ltd., M/s Shree Nakoda Ispat Ltd., M/s SKS Ispat & Power Ltd., and M/s Vandana Global Ltd., in Raipur commissionerate, availed of cenvat credit of duty paid on iron ore, iron ore pellets and chrome ore concentrate. These products were chargeable to nil rate of duty. The duty, thus, paid by the assessees of their own volition was in contravention of the provisions of section 5A mentioned above and was to be treated as deposits with the Government for which they were not entitled to avail credit. Thus, the incorrect credit of ₹ 7.45 crore availed during the years 2005-06 and 2007-08 needed to be recovered.

On the observation being pointed out (between April 2008 and April 2009), the department stated (between October 2008 and March 2009) that the Cenvat Credit Rules do not restrict a manufacturer from availing of the credit of duty paid as all the conditions laid down are fulfilled.

The reply of the department was not in consonance with section 5A (1A) and the Board's clarification of 4 January 1991.

Recommendation No. 7

- *The Government may consider issuing instructions to control and restrict the availing of cenvat credit by downstream units in cases of overpayment of duty.*

In the exit conference, the Board agreed to issue clarification on this issue. It stated that the matter would be discussed with field formations and wherever intentional passing on of credit was found, the excess credit would be reversed.

3.2 Utilisation of cenvat credit for payment of tax on input services

Rule 3(4) of the Cenvat Credit Rules stipulates that the cenvat credit may be utilised for the payment of service tax on any output service. Board has also clarified (22 August 2007) that cenvat credit cannot be utilised for payment of tax on input services.

We observed that some assessees availed cenvat credit on GTA services and services received from foreign service providers. They also utilised the cenvat

credit for payment of tax on these input services received on subsequent occasions, which was not permitted as per rules.

We found that 32 assessees in 19 Commissionerates utilised cenvat credit of ₹ 4.35 crore for the payment of service tax on GTA services received and similarly 6 assessees in 6 commissionerates utilised cenvat credit of ₹ 1.95 crore for the payment of service tax as recipient of technical services, banking and financial services, management and scientific consultancy services, intellectual property right services from foreign agencies. Since these were input services, the payment from the credit account was irregular.

On the observations being pointed out (between May 2007 and April 2009), the department accepted (between August and April 2009) audit observations of ₹ 4.33 crore in 20 cases and reported recovery of ₹ 92.65 lakh (including interest) in nine cases. In 12 other cases, it reported issue of show cause notices for ₹ 2.60 crore. However, in two cases (Nagpur and Raipur commissionerates) it stated (September 2008) that credit was admissible in view of CESTAT judgement in the case of M/s Nahar Export Ltd. {2008 (9) STR 252 (T) Delhi}. This reply was inconsistent with the Board's clarification (22 August 2007) denying use of cenvat credit for payment of tax on input services. Reply in the remaining cases had not been received (December 2010).

Recommendation No. 8

- *In view of different stands taken by different commissionerates, the Board may clarify the issue.*

In the exit conference, the Board agreed to examine different stands taken by field formations and to issue necessary clarification so that a uniform practice was followed.

3.3 Irregular utilisation of cenvat credit for paying cess and duty

Under the Cenvat Credit Rules, 2004, credit of education cess (EC), secondary and higher education cess (SHE) and national calamity contingent duty (NCCD) can be utilised only for payment of education cess, secondary and higher education cess and national calamity contingent duty respectively. The cenvat credit of customs duty is not admissible as this is not specified under the rules.

We found that 63 assessees, in 20 commissionerates, had incorrectly utilised credit of excise duty for payment of NCCD, and credit of EC for payment of SHE cess and service tax. Also credit of customs duty was availed, which was not permissible. The credit aggregating ₹ 89.11 crore was utilised incorrectly. The department had accepted audit observations in 20 cases involving ₹ 71.80 lakh and reported recovery of ₹ 97.67 lakh in 35 cases.

Two such cases are illustrated below: -

3.3.1 M/s Maruti Suzuki India Ltd., in Gurgaon commissionerate, was required to pay NCCD of ₹ 347.48 crore on the final products cleared during the years from 2005-06 to 2007-08. Against this amount, the assessee paid ₹ 265.58 crore in cash (PLA), ₹ 3.80 crore from NCCD credit account and balance of ₹ 78.10 crore from cenvat credit of excise duty. Thus, the utilisation of cenvat credit of excise duty of ₹ 78.10 crore for payment of NCCD was irregular and it was to be paid in cash.

On the audit observation being pointed out (October 2005 and January 2009), the department reported (November 2006 to October 2008) issue of three show cause notices for recovery of ₹ 113.91 crore for the period from November 2005 to August 2008.

3.3.2 M/s Jindal Stainless Ltd., and M/s Paradeep Port Trust in Bhubaneshwar I commissionerate, M/s KEL Manila in Cochin commissionerate, M/s Fenoplast Ltd., in Hyderabad I commissionerate, M/s Uni Ads Pvt. Ltd., in Hyderabad II commissionerates and M/s ACC Ltd., Lakheri, in Jaipur I commissionerate availed of cenvat credit of education cess amounting to ₹ 40.50 lakh between the period from June 2005 and March 2008. These assessees utilised the credit for payment of secondary higher education cess / service tax / excise duty which was incorrect.

On this being pointed out (between April 2008 and March 2009), M/s KEL Manila and M/s ACC Ltd. Lakheri paid an amount of ₹ 6.40 lakh including interest. The department accepted (April 2009) audit observation in the case of M/s Uni Ads Pvt. Ltd and M/s. Paradeep Port Trust and reported (April 2009/March 2009) recovery of ₹ 8.02 lakh. In the case of M/s. Fenoplast Ltd. (Unit II), the department partially accepted the observation and reported that the availing of education cess and secondary and higher education cess was inadmissible with effect from 12 May 2007, so it would direct the assessee for reversal of the cenvat amount utilised after May 2007. Further reply of the department was awaited (December 2010).

3.4 Utilisation of credit for non-specified purposes like pre-deposit, arrears etc.

Rule 3(4) of the Cenvat Credit Rules, 2004 stipulates that the cenvat credit can be utilised for payment of

(i) any duty of excise on any final product; or
(ii) an amount equal to cenvat credit taken on inputs if such inputs are removed as such or after being partially processed; or
(iii) an amount equal to cenvat credit taken on capital goods are removed as such; or
(iv) an amount under sub-rule (2) of rule 16 of the Central Excise Rules 2002; or
(v) service tax on any output service.

We found that eight assessees in six commissionerates had wrongly utilised cenvat credit of ₹ 18.43 crore for payment of arrears or for pre-deposit or for meeting judicial requirements. The department had accepted audit

observations in three cases involving credit of ₹ 21.47 lakh and reported reversal of the entire amount.

An illustrative case is detailed below: -

3.4.1 M/s Viceroy Hotels Ltd., Hyderabad, in Hyderabad II commissionerate, engaged in providing services of mandap keeper, dry cleaning, health club etc., paid part of the service tax payable on due dates through cenvat credit account and showed the remainder of ₹ 12.45 lakh as minus balance in the returns for the month of November 2007 and December 2007. This minus balance was subsequently adjusted after accrual of input credits at the end of January 2008 which was irregular. The entire amount of arrears of service tax for the above two months amounting to ₹ 12.45 lakh was irregularly adjusted against the credit of January 2008 and was required to be recovered with interest.

When we pointed this out (January 2009), the department accepted the audit observation and intimated that the assessee had paid service tax of ₹ 12.45 lakh along with interest of ₹ 1.96 lakh.

New Delhi **(SUBIR MALLICK)**
Dated : **Principal Director (Indirect Taxes)**

Countersigned

New Delhi **(VINOD RAI)**
Dated : **Comptroller and Auditor General of India**