

CHAPTER V CENVAT CREDIT

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CHAPTER V CENVAT CREDIT

Under the Cenvat Credit Rules, 2004, the credit availed on service tax paid on input services and central excise duty paid on inputs and capital goods can be utilised for payment of central excise duty on finished goods or service tax payable on output services subject to fulfilment of certain conditions. We noticed some cases of incorrect grant of cenvat credit involving ₹ 5.06 crore of service tax which are described in the following paragraphs. We communicated these observations to the Ministry through six draft audit paragraphs. The Ministry/department had accepted (December 2011) the audit observations in two draft audit paragraph with money value of ₹ 1.46 crore.

5.1 Cenvat credit utilised for payment of tax on input services

Under the provisions of rule 3(4)(e) of the Cenvat Credit Rules, 2004, cenvat credit can be utilised for payment of service tax only on output services.

5.1.1 M/s Thermax Ltd., in Pune I commissionerate, availed cenvat credit of ₹ 1.92 crore on various input services. The assessee utilised this credit to pay service tax on the input services received from various foreign service providers during the period April 2005 to March 2008. The utilisation of cenvat credit of ₹ 1.92 crore for inputs services was irregular, which was recoverable in cash alongwith interest.

When we pointed this out (December 2008), the Ministry did not admit (December 2011) the audit observation and stated that the services received from foreign service providers were input services for the assessee, hence, cenvat credit of tax paid on these services was admissible to the assessee.

The reply of the Ministry supports our contention that these services were input services for the assessee. Hence the cenvat credit on the tax paid were admissible but only for paying service tax on output services. In the instant case, the cenvat credit was used to pay service tax on input services, which was not admissible.

5.1.2 M/s ISMT Ltd., in Pune III commissionerate, utilised cenvat credit of ₹ 22.13 lakh during April 2006 to March 2007 for payment of service tax towards the goods transport agencies services availed for inward transport of inputs/capital goods. As these services were input services, the utilisation of cenvat credit of ₹ 22.13 lakh for these input service was irregular, which was recoverable in cash alongwith interest.

When we pointed this out (February 2011), the Commissionerate stated (June 2011) that since GTA service had been omitted from output service definition from 1st March 2008, the same had to be treated as output service for the period prior to 2008. Further, the Commissionerate had referred to decision held in Asian Tubes Ltd. {(2010 (19) STR 315 (Commr. Appeal)} where it was held in view of the explanation to rule 2(p) of Cenvat Credit Rules, 2004, effective prior to 19 April 2006, that the manufacturer service recipient was a deemed service provider and any service provided by him was to be deemed

as an output service and that the cenvat credit availed towards the payment of service tax was in accordance with law.

The decision quoted by the Commissionerate was not applicable in the instant case, as the period of objection pertained to the period April 2006 to March 2007 and the said explanation was done away vide notification 8/2006/CE dated 19 April 2006. Further, the reply of the Commissionerate was at variance with Board circular (23/8/2007) which clarified that the service provided by a Goods Transport Agent (GTA) for which the consignor or consignee is made liable to pay service tax does not become an 'output service' for such consignor or consignee and that the payment of such service tax cannot be made through credit accumulated by such consignor or consignee.

The reply of the Ministry had not been received (December 2011).

5.2 Cenvat credit of service tax paid on transportation services beyond the place of removal

Under rule 2(l) of Cenvat Credit Rules, 2004, input service means any service (i) used by a provider of taxable service for providing an output service, or (ii) used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products upto the place of removal and includes services used in relation to setting up, modernisation, renovation or repairs of a factory, premise of provider of output service or an office relating to such factory or premises, inward transportation of inputs or capital goods and outward transportation upto the place of removal.

Under the provisions of rule 3 of the Cenvat Credit Rules, 2004, a manufacturer is allowed to take credit of service tax paid on any 'input service' used in the manufacture of final goods. Service tax paid by the manufacturer for outward transportation of final products beyond the place of removal is not an input service and credit of tax paid on such service is not admissible.

5.2.1 M/s Vedanta Aluminium Ltd., Langigarh a manufacturer of Calcined Alumina in Bhubaneswar I commissionerate, had availed cenvat credit of ₹ 1.30 crore towards service tax paid during the period between April 2008 and March 2010 on certain services like construction service viz., construction of barrack and hostel at civil township and outdoor catering services. The availing of service tax credit on these services was incorrect as these fell outside the scope of input service and had no nexus with process of manufacture of final products.

When we pointed this out between (April and October 2010) the Ministry accepted (October 2011) the audit observation and stated that show cause notice was under process of issue.

5.2.2 M/s PSL Ltd., Phagi in Jaipur I commissionerate, availed exemption on spirally welded M S Pipes supplied to 'Bisalpur Water Supply Project'

financed by the Asian Development Bank. Scrutiny of records revealed that the original contract of manufacture and supply of spiraled M S pipes for the Project was awarded to M/s Larsen & Toubro Ltd., Chennai who subsequently sub contracted this work to the assessee. The main contractor agreed for free supply of principal raw material HR coil to the sub contractor and the subcontractor carried out entire manufacture of spirally welded M S pipes on behalf of the main contractor. As per terms and conditions of agreement entered between the assessee (sub contractor) and M/s Larsen & Toubro Ltd., Chennai (Main contractor), service tax paid by the assessee on transportation of H.R coil would be reimbursed by the main contractor. Consequently the assessee got reimbursement of service tax paid by him amounting to ₹ 30.65 lakh (service tax ₹ 29.76 lakh, education cess ₹ 0.59 lakh and SHE cess ₹ 0.30 lakh) from main contractor by raising invoices and also availed cenvat credit thereof.

Since the assessee got reimbursement of service tax paid by him on GTA service from main contractor, the assessee was not entitled to avail cenvat credit thereof by treating it as input service as this was input service only for the main contractor. Interest under rule 14 of the Cenvat Credit Rules, 2004, was also to be recovered.

When we pointed this out (February 2011), the Commissionerate stated (May 2011) that the assessee had correctly taken cenvat credit of service tax paid by him through challan on transportation of inputs as the inputs were used by them in the manufacture of final products. The reply of the Commissionerate is not acceptable to audit as the service tax paid by the assessee on transportation of inputs was reimbursed by the main contractor. Therefore the assessee was not entitled to avail cenvat credit of service tax on GTA service as this was an input service for the main contractor.

The reply of the Ministry had not been received (December 2011).

5.3 Separate account for common input services used in taxable/exempted services not maintained

As per rule 6(2) of the Cenvat Credit Rules, 2004 where a provider of output service avails of cenvat credit in respect of any input services and provides such output services which are chargeable to tax as well as exempted from service tax, then the provider of output service shall maintain separate accounts for input services meant for use in providing output service and quantity of input services used in the exempted services. Further as per rule 6(3) of said Cenvat Credit Rules, provider of output services opting not to maintain separate accounts shall have an option either to pay an amount equal to eight per cent of the value of exempted service under rule 6(3)(i) 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 for provision of exempted services under rule 6(3)(ii) after compulsorily intimating in writing to the Superintendent of Central Excise and pay provisionally for every month under rule 6(3A).

M/s Tata Consulting Engineers Ltd., in Mumbai I service tax commissionerate, provided taxable as well as exempted services during the 2008-09 and 2009-10 but had not maintained separate accounts of cenvat credit availed on inputs/input services. The assessee had neither exercised the option to pay an amount equal to 8 per cent (five per cent with effect from July 2009) of the value of exempted services nor did the assessee pay an amount equivalent to the cenvat credit attributable to inputs and input services used in or in relation to the provision of exempted services. The total exempted services provided during the period April 2008 to September 2009 was ₹ 14.96 crore. Therefore the assessee was liable to pay ₹ 1.15 crore (being 8 per cent of the value of the exempted services during April 2008 to June 2009 and 5 per cent during July 2009 to September 2009).

When we pointed out (March 2010), the assessee intimated (April 2010) the Commissionerate about opting for payment of amount equivalent to the cenvat credit attributable to inputs/input services used in or in relation to provision of exempted output service subject to conditions and procedure specified in Rule 6(3A). Accordingly assessee paid ₹ 14.05 lakh under Rule 6(3A)(h) read with Rule 6(3A)(c) and ₹ 2.53 lakh towards interest calculated as per Rule 6(3A)(i).

The Commissionerate had not issued any show cause notice and this issue was not observed by internal audit conducted during December 2009. Reply was awaited from the Commissionerate (December 2011).

The reply of the Ministry had not been received (December 2011).

5.4 Premature availing of cenvat credit on input services

Rule 4(7) of the Cenvat Credit Rules, 2004, provides that cenvat credit of tax paid on input services shall be allowed, on or after the day on which payment is made for the input service and service tax. Further, rule 14 of the rules *ibid*, provides that where the cenvat credit has been taken or utilised wrongly, the same alongwith interest shall be recovered from the manufacturer or the provider of output service.

M/s Gwalior Chemical Industries Ltd., Nagada, in Indore commissionerate, availed cenvat credit of service tax paid on various input services on 31 August 2009. The payment of value of these input services including service tax was made in the subsequent month i.e. from 2 September 2009 to 21 September 2009. As the cenvat credit was availed before the payment of value of service charges, therefore, the cenvat credit of ₹ 16.24 lakh was wrongly availed, which was recoverable alongwith interest and penalty.

When we pointed this out (October 2010) the Commissionerate stated that the assessee had agreed to pay the amount. Further reply was awaited (December 2011).

The reply of the Ministry had not been received (December 2011).