



**Report of the
Comptroller and Auditor General of India
for the year ended March 2016**



Cenvat credit scheme

Union Government
Department of Revenue
Indirect Taxes – Central Excise and Service Tax
Report No. 10 of 2016

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Preface

This Report has been prepared for submission to the President of India under Article 151 of the Constitution of India.

The Report contains significant results of the performance audit on Cenvat credit scheme and covers the period from 2012-13 to 2014-15. Matters relating to subsequent periods have also been included, wherever necessary.

The instances mentioned in this Report are those which came to notice in the course of test audit conducted during the period 2015-16.

The audit has been conducted in conformity with the Auditing Standards issued by the Comptroller and Auditor General of India.

Audit wishes to acknowledge the cooperation received from the Department of Revenue, Central Board of Excise and Customs and its field formations at each stage of the audit process.

Executive summary

We conducted the Performance Audit on Cenvat credit scheme, to seek an assurance that provisions in the Act/rules/clarifications/procedures as laid down are unambiguous and adequate to safeguard any misuse of the Cenvat credit scheme and that the internal control and monitoring mechanism were in place and effective. The Performance Audit was conducted in 41 selected Commissionerates which included examination of records relating to 469 assessees.

The Performance Audit revealed certain inadequacies in the extant provisions, both of system as well as deficiencies in internal controls relating to the Cenvat credit scheme.

- a. We observed that the proportionate value of service tax credit on input services of ₹ 21.63 crore was not reversed due to absence of suitable provision in Cenvat Credit Rules, 2004.

(Paragraph 2.2)

- b. We observed that concessional rate of duty in respect of mobile phones, allowing benefit of Cenvat credit in respect of input services even though it was meant to be restricted to inputs and capital goods resulted in unintended benefit of ₹ 7.30 crore to the assessee.

(Paragraph 2.3)

- c. During test check we observed in three cases where goods were declared as obsolete but Cenvat credit was not reversed due to absence of suitable provisions.

(Paragraph 2.4)

- d. We observed that there is no provision for charging interest in case of non/delayed reversal of Cenvat credit in respect of non/delayed receipt of goods sent to job worker.

(Paragraph 2.5)

- e. We observed instances of non-submission of various prescribed returns by the assessees. Non-submission of returns would hinder the department's ability to verify the duty paid by assessees, correctness of valuation, availing of Cenvat credit, admissibility of exemption, etc.

(Paragraph 3.1)

- f. In violation of the existing instructions 21 out of selected 41 Commissionerates had not conducted any detailed scrutiny of the returns. The reply from the remaining 20 Commissionerates is still awaited.

(Paragraph 3.2)

- g. We observed various shortcomings while examining adherence to the rules and regulations of Cenvat Credit Rules, 2004 involving ₹ 128.31 crore which failed to come to the notice of the department due to non-observance of the compliance verification mechanism as envisaged.

(Chapter 4)

Summary of Recommendations

1. *The Ministry may insert a provision in Cenvat Credit Rules, to reverse the proportionate Cenvat credit of input services at the time of clearance of input/capital goods.*
2. *Government may consider making suitable amendment to the Notification to restrict credit on input services.*
3. *The government may consider inserting provision for reversal of Cenvat credit where the inventories were declared as obsolete but were not written off from the books of accounts and where capital goods after being used are written off but not removed from the factory.*
4. *The Government may consider inserting provision for charging interest in case of non/delayed reversal of Cenvat credit in respect of non/delayed receipt of goods sent to job worker.*
5. *The government may consider inserting provision for furnishing detailed information regarding Cenvat credit availed by the assessee containing invoices/documents nos., date of invoices, name of goods with chapter heading, amount of credit taken etc. so that preliminary check may be exercised at Range level.*

Chapter 1 : Introduction

1.1 Background

A new mode of central excise taxation procedure called Modvat (Modified Value Added Tax) was introduced from 1 March 1986 to implement one of the measures contemplated in the long term fiscal policy announced by the Government in December 1985.

The scheme enables manufacturers to avail credit of duty paid on the inputs (from the year 1986) and capital goods (from the year 1994) and utilise such credit for payment of duty on the final products manufactured by them. The scheme was renamed as Cenvat Credit Scheme with effect from 1 April 2000. This was replaced by Cenvat Credit Rules, 2001 effective from 1 July 2001 which simplified Cenvat provisions and procedures for allowing credit of duty paid on specified inputs and capital goods used in or in relation to the manufacturer of specified final products. Further revision the rules were made through Cenvat Credit Rules, 2002 with effect from 1 March 2002.

The Central Government introduced the levy of tax on services from the year 1994. With amendment to Section 94(2) of Finance Act, 1994 in the year 2002, giving powers to Central Government to make rules relating to credit of Service Tax (ST). Central Government introduced Service Tax Credit Rules, 2002 with effect from 16 August 2002. This scheme was similar to Cenvat scheme on excise but was limited only to credit on input service used in providing taxable output services. Cenvat Credit Rules, 2004, have been introduced and made effective from 10 September 2004 so that credit of input duties and tax can be extended across goods and services.

1.2 Organisational set up

Central Board of Excise and Customs (CBEC) set up under the Central Boards of Revenue Act, 1963 is a part of the Department of Revenue under the Ministry of Finance, Government of India. It deals with the tasks of formulation of policy concerning levy and collection of Customs, Central Excise duties and Service Tax, prevention of smuggling and administration of matters relating to Customs, Central Excise, Service Tax and Narcotics. The Board is the administrative authority for its subordinate organisations, including Custom Houses, Central Excise and Service Tax Commissionerates and the Central Revenues Control Laboratory.

1.3 Legal provisions

1.3.1 Section 37 of Central Excise Act, 1944, empowers the Central Government to make rules inter alia to:

- (i) provide for the credit of duty paid or deemed to have been paid on the goods used in or in relation to the manufacture of excisable goods;
- (ii) provide for credit of service tax leviable under Chapter V of Finance Act, 1994 paid or payable on taxable services used in, or in relation to, the manufacture of excisable goods;
- (iii) provide for the giving of credit of sums of money with respect to the raw materials used in the manufacture of excisable goods.

1.3.2 Section 94 of the Finance Act, 1994, empowers the Central Government to make rules for credit of service tax paid on the services consumed or duties paid or deemed to have been paid on goods used for providing a taxable service.

1.4 Utilisation of Cenvat credit for payment of duty

In the scheme of availing Cenvat credit and utilising it for payment of duty/tax, payment from Cenvat credit represents duty/tax already paid on inputs and input services used in the manufacture of goods or provision of service. Table 1 shows trend of Central Excise (CE) collections through Personal Ledger Account (PLA) and Cenvat credit during the period of review.

**Table 1: Trend of central excise collection through PLA and Cenvat credit
for period 2012-13 to 2014-15**

Year	No. of assessees	CE duty paid through PLA		CE duty paid through Cenvat credit		(₹ in crore) CE duty paid from Cenvat credit as % of PLA payments
		Amount	% change over previous year	Amount	% change over previous year	
2012-13	4,09,139	1,75,845	--	2,58,697	--	147.12
2013-14	4,35,213	1,69,455	-3.63	2,73,323	5.65	161.30
2014-15	4,67,286	1,89,038	11.56	2,91,694	6.72	154.30

Source : Figures furnished by the Ministry.

Table 2 shows trend of service tax collections through PLA (cash) and Cenvat credit during the period of review.

**Table 2: Trend of service tax collection through PLA and Cenvat credit
for period 2012-13 to 2014-15**

Year	No. of assessees	Service tax paid through PLA		Service Tax paid through Cenvat credit		ST paid from Cenvat credit as % of PLA payments
		Amount	% change over previous year	Amount	% change over previous year	
2012-13	19,82,297	1,32,601	--	5,507	--	4.15
2013-14	22,58,599	1,54,780	16.72	15,090	174.01	9.74
2014-15	25,11,728	1,67,969	8.52	14,404	-4.54	8.57

Source : Figures furnished by the Ministry.

1.5 Why we chose this topic

Keeping in view significant amount of duty/tax paid through Cenvat in last three years, various changes in recent years such as restriction to take Cenvat credit within six months (from September 2014)/within one year (from March 2015) and a large number of cases of irregular availment/utilisation of Cenvat credit observed during our regular audit, it was felt necessary to evaluate the adequacy of the existing provisions and effectiveness of implementation and monitoring mechanisms.

1.6 Audit Objectives

The Performance Audit was conducted to seek assurance whether:

- a) provisions in the rules/clarifications/procedures as laid down are unambiguous and adequate to safeguard any misuse of the scheme;
- b) internal control and monitoring mechanism were in place and effective; and
- c) departmental administration was efficient in implementing and ensuring compliance with the rules and regulations as laid down in the Cenvat Credit Rules, 2004, and other related rules.

1.7 Scope of audit and coverage

We selected 20 per cent of Commissionerates/Divisions/Ranges (CDR) and all the five Large Taxpayer Unit (LTU) Commissionerates. While doing so the CDRs having maximum number of assessees paying duty more than ₹ one crore per annum through Cenvat credit were selected. Thus, we selected and covered 41¹ out of 145 Commissionerates, 68 out of 737 divisions, 129 out of 3,649 ranges and 469 out of 4,54,080 assessees from the selected Commissionerates. Within the selected CDRs all assessees paying duty/tax of more than ₹ three crore through Cenvat credit, 50 per cent assessees paying duty/tax amount of between ₹ one to three crore and 20 per cent assessees paying duty/tax amount of upto ₹ one crore through Cenvat credit per annum were selected. The period of examination of this performance audit is from 2012-13 to 2014-15.

1.8 Acknowledgement

We acknowledge the co-operation extended by Central Board of Excise and Customs (CBEC) and its subordinate formations, in providing the necessary records for the conduct of this audit.

We discussed the audit objectives and scope of the performance audit in an entry conference with CBEC officers on 28 April 2015 and exit conference was held on 4 March 2016. The Ministry furnished the reply in February and April 2016 which are included in this report.

¹ Ahmedabad-III, Alwar, Bengaluru LTU, Bengaluru-I, Bharuch, Bhubaneswar-I, Bhubaneswar-II, Bilaspur, Bolpur, Chandigarh-I, Chennai LTU, Chennai-III, Dehradun, Delhi LTU, Delhi-I, Delhi-I ST, Faridabad-II, Ghaziabad, Guwahati, Gwalior, Hyderabad-III, Hyderabad-IV, Indore, Jaipur, Jamshedpur, Kochi, Kolkata LTU, Kolkata-I ST, Mumbai LTU, Noida ST, Noida-I, Patna, Pune-III, Raigad, Raipur, Ranchi, Silvassa, Mumbai-II ST, Mumbai-VII ST, Thane-I and Thiruvananthapuram

Chapter 2: System issues

2.1 Utilisation of Cenvat credit for payment of duty

2.1.1 It is observed from Table 1 that central excise duty paid through Cenvat as a percentage of PLA payments is approximately 154 per cent over the period of review. Further it was found that in 13 out of 41 selected Commissionerates the central excise duty paid from Cenvat credit as percentage of PLA payment was more than double in comparison with national averages. Some other discrepancies in relation to availing and utilisation of credit were also observed. Three cases are illustrated below:-

- In Silvassa Commissionerate, duty payment through Cenvat as compared to PLA is as high as 1,300 per cent approximately during 2012-13 to 2014-15. This ratio is very high in comparison with all India figures of 154 per cent.
- In Hyderabad-III Commissionerate while the number of assessees increased from 424 in the year 2012-13 to 457 in the year 2014-15 (eight per cent) the corresponding duty payment through PLA decreased from ₹ 961 crore to ₹ 771 crore (minus 20 per cent). In respect of Cenvat utilisation it increased from ₹ 1,182 crore to ₹ 1,207 crore (two per cent).
- In Ahmedabad-III Commissionerate during the years 2013-14 and 2014-15 though the number of assessees increased from 2,012 to 4,452 (121 per cent) the corresponding duty payment through PLA increased from ₹ 838 crore to ₹ 920 crore (10 per cent) and in respect of Cenvat utilisation it increased from ₹ 3,051 crore to ₹ 3,170 crore (four per cent) only.

2.1.2 It is observed from Table 2 that service tax paid through Cenvat as a percentage of PLA payments is approximately seven per cent over the period of review. Further it was found that in 14 out of 41 selected Commissionerates payment from Cenvat credit as percentage of PLA payment, was more than double in comparison with national averages. Two cases are illustrated below:-

- In Bengaluru LTU Commissionerate the utilisation of Cenvat credit during 2012-13 and 2013-14 were 58 and 61 per cent respectively which is more than seven times in comparison with all India average of 7.48 per cent.

- In Bhubaneswar-I Commissionerate the utilisation of Cenvat credit during the year 2012-13 and 2013-14 were 76 and 67 per cent respectively which is more than nine times in comparison with all India average of 7.8 per cent.

2.2 Absence of provision to reverse credit of service tax paid on input services used for inputs removed as such

As per rule 2(l) of the Cenvat Credit Rules, 2004, “input service” includes services used in relation to procurement of inputs and inward transportation of inputs or capital goods and outward transportation upto the place of removal etc. Further, rule 3 (1) of the rules, ibid, provides that the manufacturer or producer of final products or provider of taxable service shall be allowed to take credit of service tax on input service received by the manufacturer of final product. Although rule 3(5) provides for reversal of credit taken on inputs or capital goods removed as such, there is no corresponding provision under the rules requiring payment of the amount equal to the credit of service tax paid on input services. These services could include custom house agent’s services, clearing and forwarding agents’ services, transportation availed for procurement/transportation of inputs or capital goods etc. Non-existence of such provision resulted in unintended benefit to the manufacturer.

During test check of records of 44 cases in 17 Commissionerates, we observed that the proportionate value of service tax credit on input services of ₹ 21.63 crore was not reversed due to absence of suitable provision in Cenvat Credit Rules, 2004. A few cases are illustrated below:-

2.2.1 M/s. UPL Ltd. (Unit-V) in Bharuch Commissionerate, cleared inputs as such of ₹ 139.21 crore out of total inputs purchased during the period of review worth ₹ 1,459.10 crore. However, the assessee, due to absence of provision for reversal of Cenvat credit on input services involved in inputs cleared as such, did not reverse the same. This resulted in unintended benefit of ₹ 5.96 crore to the manufacturer during the aforesaid period.

2.2.2 M/s. Toyota Kirloskar Motors Pvt. Ltd., in Bengaluru LTU Commissionerate, cleared inputs as such of ₹ 6.82 crore out of total inputs purchased during the period of review worth ₹ 950.36 crore. However, the assessee, did not reverse the credit of input services involved in inputs cleared as such. This resulted in unintended benefit of ₹ 3.60 crore to the manufacturer during the aforesaid period.

2.2.3 M/s. Kirloskar Oil Engines Ltd. and M/s. Cummins India Ltd., in Pune-III Commissionerate, cleared inputs as such of ₹ 271.15 crore out of total

inputs purchased during the period of review. However, the assessee, did not reverse the credit of input services. This resulted in unintended benefit of ₹ 4.78 crore to the manufacturer during the aforesaid period.

2.2.4 M/s. Asian Paints Ltd., in Mumbai LTU Commissionerate, cleared inputs as such of ₹ 76.91 crore out of total inputs purchased during the period of review. Due to absence of provision for reversal of Cenvat credit on input services involved in inputs cleared as such the assessee, did not reverse the same. This resulted in unintended benefit of ₹ 1.23 crore to the manufacturer during the aforesaid period.

When we pointed this out (between April and June 2015), the Ministry stated that this is a policy matter.

Recommendation No.1

The Ministry may insert a provision in Cenvat Credit Rules, to reverse the proportionate Cenvat credit of input services at the time of clearance of input/capital goods as such.

During the exit conference, the Ministry stated that a survey will be undertaken to find out misuse, if any. The result of this survey will be shared with the CAG.

2.3 Lacunae in provision allowing credit on input services

While amending Notification dated 17 March 2012, the notification dated 1 March 2015 allowed clearance of mobile phones with payment of duty at the rate of one per cent subject to conditions as specified therein which restricted availing of Cenvat credit in respect of inputs and capital goods only. The condition remained silent in respect of availing of Cenvat credit on input services. As the notification allowed concessional rate of duty in respect of mobile phones, allowing benefit of Cenvat credit in respect of input services does not appear to be in line with basic principles of Cenvat credit scheme.

M/s. Samsung India Electronic Pvt. Ltd., in Noida-I Commissionerate, engaged in manufacture of mobile handsets, cleared mobile phones with payment of duty at the rate of one per cent availing the benefit of the aforementioned notification and also availed Cenvat credit in respect of input services during March 2015. As the mobile phones were cleared at concessional rate of duty, availing of Cenvat credit in respect of input services by the manufacturer resulted in unintended benefit of ₹ 7.30 crore during March 2015.

When we pointed this out (June 2015), the Ministry stated that this is a policy matter.

Recommendation No.2

Government may consider making suitable amendment to the Notification to restrict credit on input services as well.

During the exit conference the Ministry stated that the issue is under examination of Tax Research Unit (TRU) and detailed reply will be furnished separately.

2.4 Absence of provision for credit reversal for obsolete goods

Rule 3 of Cenvat Credit Rules, 2004, provides that a manufacturer or a provider of output service shall be allowed to take credit of input or input services or capital goods for use in or in relation to the manufacture of final products or for providing output services.

Rule 3(5A) of Cenvat Credit Rules, 2004, provides that when the capital goods, on which Cenvat credit has been taken, are removed after being used, whether as capital goods or as scrap or waste, the manufacturer or provider of output services shall pay an amount equal to the Cenvat credit taken on the said capital goods reduced by the percentage points calculated by straight line method as specified in the rule for each quarter of a year or part thereof from the date of taking the Cenvat credit. But if the amount so calculated is less than the amount equal to the duty leviable on transaction value, the amount to be paid shall be equal to the duty leviable on transaction value.

According to rule 3(5B) of Cenvat Credit Rules, 2004, 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 off 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. But, there is no provision for goods declared as obsolete but not written off in accounts. During test check we observed in three cases where goods were declared as obsolete but Cenvat credit was not reversed which are illustrated below:-

2.4.1 M/s. Rashtriya Ispat Nigam Ltd., in Kakinada Commissionerate, had made the provision of ₹ 36.36 crore against the cumulative stock of obsolete material. In the absence of provision, the assessee had not reversed the Cenvat credit of ₹ 4.49 crore attributable to these obsolete material.

2.4.2 M/s Toyota Kirloskar Motors Pvt. Ltd., in Bangalore LTU Commissionerate, declared some of the used capital goods as obsolete in the books of accounts and the same were kept in the factory without removal.

However, due to absence of provisions, the assessee did not pay the amount equal to Cenvat credit of ₹ 24.29 lakh on the ground that the said goods had not been removed from the factory.

2.4.3 Similarly M/s. HMT Machine Tools Ltd., in Hyderabad-IV Commissionerates, had not reversed the Cenvat credit of ₹ 26.45 lakh attributable to obsolete material declared in the books of accounts.

When we pointed this out (between April and July 2015), the Ministry stated (February 2016) that it is a policy matter.

Recommendation No.3

The government may consider inserting provision for reversal of Cenvat credit where the inventories were declared as obsolete but were not written off from the books of accounts and where capital goods after being used are written off but not removed from the factory.

The Ministry in its reply stated (February 2016) that the issue is under examination.

2.5 Absence of provision for charging interest on reversal of credit for non-receipt/delayed receipt of goods sent for job work within 180 days

Inputs or semi finished goods sent to job worker under rule 4(5) (a) of Cenvat Credit Rules, 2004, should be returned to the factory within 180 days. For failure to do so proportionate Cenvat credit on inputs/semi finished goods not received back is required to be reversed. However, in case of delay in reversal of credit, there is no specific provision for charging interest on such delayed reversal. This results in loss of interest to the Government.

M/s. LanXESS India Pvt. Ltd., in Bharuch Commissionerate, had not received back inputs/capital goods involving credit of ₹ 19.78 lakh sent to job worker ever after expiry of 180 days. The assessee reversed the Cenvat credit on 1 June 2015. Due to absence of provision to charge interest on non-reversal or delayed reversal of Cenvat credit in respect of non-receipt/delayed receipt of goods sent to job worker resulted in loss of interest of ₹ 3.17 lakh.

When we pointed this out (June 2015), the Ministry stated (February 2016) that it is a policy matter.

Recommendation No.4

The Government may consider inserting provision for charging interest in case of non/delayed reversal of Cenvat credit in respect of non/delayed receipt of goods sent to job worker.

During exit conference Ministry replied that Tariff Conference held on 28 and 29 October 2015 have already decided that the interest is liable to be paid after the expiry of period of 180 days from the date of issue of capital goods to job worker and same principle would also apply in case of inputs sent to job worker and there is no need for insertion of provision for charging interest.

On one hand Ministry stated that it is a policy matter (Para 2.5) and on the other hand it stated (Exit conference) that the tariff conference had already clarified the issue and no need for insertion of provision for charging interest.

Audit is of the opinion that to avoid ambiguity there is a need to insert specific provision in this regard.

Chapter 3 : Internal control

The department has three methods of internal controls viz. scrutiny, audit and anti-evasion, for ensuring compliance with all legislations and rules relating to levy and collection of excise duty/service tax including rules made for Cenvat credit scheme. Keeping in view the system of self assessment the department controls the non/short levy of duty or erroneously refunds through issuance of show cause notices and confirming the same through adjudication process.

3.1 Submission of returns

As per central excise statute a manufacturer is required to file various returns viz. ER-1, ER-2, ER-3, ER-4, ER-5, ER-6, ER-7 and ER-8. Further, as per service tax statute the assessee is required to file ST-3 return.

A monthly return for production and removal of goods and other relevant particulars and Cenvat credit in the form of ER-1 by 10th of the following month is to be submitted by a manufacturer those who are not eligible for Small Scale Industries (SSI) concession.

An annual return regarding information relating to principal inputs in the form of ER-5 is to be submitted by the assessees paying duty of ₹ one crore or more per annum (either through PLA or Cenvat or both together) for the previous financial year and those manufacturing goods falling under specified chapters and headings by 30th April every year for the current financial year.

A monthly return of receipt and consumption of each of principal inputs by 10th of the following month by those assessees required to submit ER-6.

A half yearly return of taxable services provided in the form of ST-3 is to be submitted by the person liable to pay service tax within 25 days from close of half year.

During test check we observed some discrepancies in filing of various returns which are narrated below:-

3.1.1 ER-1 and ST-3 returns

As per sub-rules (7) and (9) of rule 9 of Cenvat Credit Rules, 2004, the manufacturer and service provider availing Cenvat credit shall submit within the stipulated days a monthly (ER-1) and a half yearly return (ST-3) respectively to the superintendent of central excise. Non-submission of these returns attract penalty under rule 15A of Cenvat Credit Rules, 2004.

During scrutiny of the figures furnished by 33 selected Commissionerates we observed that 244 ER-1 returns were not submitted during the period of review, but department initiated action only in respect of 89 ER-1 returns. Three² selected Commissionerates did not furnish the information. The remaining five³ Commissionerates did not deal with central excise.

During scrutiny of the figures furnished by 32 Commissionerates we observed that 8,346 ST-3 returns were not submitted during the period 2012-15, but department initiated action only in respect of 276 ST-3 returns. Seven⁴ selected Commissionerates did not furnish the information. The remaining two Commissionerates viz., Delhi I and Noida I did not deal with service tax.

When we pointed this out (April and June 2015), the Ministry stated (February 2016) that remedial action is being initiated against the defaulters.

3.1.2 ER-5 return

As per rule 9 A (1) of Cenvat Credit Rules, 2004, all assessee (other than those who have paid less than ₹ one crore for the previous financial year and those manufacturing goods falling under specified chapters and headings) are required to file ER-5 returns which is annual information on principal inputs, by 30 April every year for the previous financial year.

We observed in selected ranges of 34 selected Commissionerates that 722 number of ER-5 returns were not submitted by the assessees during the period of review. However, the department initiated action only in 113 cases. Mumbai LTU and Raigad Commissionerates have not furnished the details. The remaining five⁵ Commissionerates did not deal with central excise.

When we pointed this out (April and June 2015), the Ministry stated (February 2016) that remedial action is being initiated against the defaulters.

3.1.3 ER-6 return

Rule 9A(3) of Cenvat Credit Rules, 2004, prescribes for submission of a monthly return of receipt and consumption of each of principal inputs in the form ER-6 return by assessees paying those who are filing ER-5 return.

We observed in selected ranges of 33 selected Commissionerates that 4,315 number of ER-6 returns were not submitted by the assessees during the period of review. However, the department initiated action only in 783 cases. Mumbai LTU, Hyderabad IV and Raigad Commissionerates have not

² Bilaspur, Gwalior and Pune III

³ Delhi-I ST, Kolkata-I ST, Mumbai-II ST, Mumbai-VII ST and Noida ST.

⁴ Bilaspur, Dehradun, Mumbai LTU, Noida-I, Pune III, Raigarh and Thane-I

⁵ Delhi-I ST, Kolkata-I ST, Mumbai-II ST, Mumbai-VII ST and Noida ST.

furnished the details. The remaining five⁶ Commissionerates did not deal with central excise.

When we pointed this out (April and June 2015), the Ministry stated (February 2016) that remedial action is being initiated against the defaulters.

Audit opines that non-submission of returns may lead to non-verification of duty payment by assessee, correctness of valuation, availing of Cenvat credit, admissibility of exemption etc. It further leads to skewed population for selection of returns for detailed scrutiny. Further, in the absence of filing of ER-5 and ER-6 the department may not be able to detect the clandestine production and removal of goods by the assessee.

During the exit conference, the Ministry stated four returns have been proposed to be discontinued from the current fiscal. It is further mentioned that difference in number of returns received corresponding to the assessee registered is due to gap in active and non-active assesses and provision to suspend registration temporarily for non active assessee is being considered actively in the Goods and Service Tax (GST) law.

3.2 Scrutiny of returns

3.2.1 Preliminary scrutiny/Review and Correction

After the introduction of Automation of Central Excise and Service Tax (ACES), preliminary scrutiny of returns is being done by the system itself. The purpose of the preliminary scrutiny is to ensure completeness of information, timely submission of returns, time payment of duty, arithmetical accuracy of the amount computed as duty, closing and opening balance of Cenvat credit etc. The range superintendent is required to verify the returns thrown by the system for review and correction. He is also required to rectify the errors, if any, in the returns in consultation with the concerned assessee.

During scrutiny of 2,580 returns in selected ranges of 41 Commissionerates we observed in two cases, in Jamshedpur and Patna Commissionerates, that there were differences in the closing balance and opening balances of Cenvat credit as per the returns furnished by the assessee. Although the system had marked the returns for review and correction, the department did not verify the differences involving availing of Cenvat credit of ₹ 14.01 lakh during the period of review. One case is illustrated below:-

M/s. TML Driveline Ltd., in Jamshedpur Commissionerate, showed the closing balance of ₹ 3.10 crore Cenvat credit in the return for the month of

⁶ Delhi-I ST, Kolkata-I ST, Mumbai-II ST, Mumbai-VII ST and Noida ST.

September 2013. However, in the return of October 2013 the opening balance of Cenvat credit was shown as ₹ 3.23 crore. Thus, there is a difference of ₹ 13 lakh, which needs examination by the department.

When we pointed this out (June 2015), the Ministry intimated (February 2016) the reversal of Cenvat credit of ₹ 13.33 lakh along with interest of ₹ 3.93 lakh.

3.2.2 *Detailed scrutiny*

The purpose of detailed scrutiny is to establish the validity of information furnished in the tax return and to ensure correctness of valuation, availing of Cenvat credit, classification and effective rate of tax applied after taking into consideration the admissibility of exemption notification availed etc. Unlike preliminary scrutiny, detailed scrutiny is to cover only certain selected returns, identified on the basis of risk parameters, developed from the information furnished in the returns submitted by the taxpayers.

Para 4B read with para 4.1A of Manual for the Scrutiny of Central Excise Returns, 2008, provides for selection of upto five per cent of total returns received for a detailed scrutiny of assessment on the basis of risk parameters. Paragraph 4.2A of the Manual for Scrutiny of Service Tax Returns, 2009 stipulates that upto two per cent of the returns need to be examined in detailed scrutiny.

The data relating all India detailed scrutiny of returns for the year 2012-13 and 2013-14 have been included vide paragraph No.1.15.2 and 1.14.2 for Central Excise and Service Tax in the Audit Report Nos.7 of 2015 and 4 of 2015 respectively. However, the details of detailed scrutiny for the year 2014-15 were not supplied by the department.

Selected ranges of 21 Commissionerates⁷ out of selected ranges of 41 Commissionerates, stated that no detailed scrutiny of returns was undertaken by them. The reply from the remaining 20 Commissionerates is still awaited.

When we pointed this out (between April and June 2015), the Ministry stated (February 2016) that the work of detailed scrutiny has been initiated and during exit conference it intimated that instructions with further modalities of undertaking detailed scrutiny has been issued in June 2015.

⁷ Ahmedabad-III, Alwar, Bharuch, Bhubaneswar-I, Bhubaneswar-II, Bilaspur, Chennai-III, Dehradun, Ghaziabad, Gwalior, Hyderabad-III, Hyderabad-IV, Indore, Kochi, Noida-I (CX), Noida ST, Patna, Raipur, Ranchi, Silvassa and Thiruvananthapuram

3.3 Verification of Cenvat credit availed

ER-1/ER-3 and ST-3 returns contain a table for details of Cenvat credit taken and utilised for furnishing information regarding various types of credit taken and its utilisation for different purposes during a month/quarter. It is very important on the part of the department to verify the amount of "credit taken" as shown in these returns with the source documents such as invoices, bill of entries etc. At present department verifies the amount of credit shown in the returns in course of detail scrutiny and internal audit of the assessees.

Scrutiny of the figures as furnished by the department⁸ regarding verification through detailed scrutiny and internal audit done by department of Cenvat credit availed by the assessees falling under the selected ranges, revealed that during the period of review on an average of 33.67, 30.47 and 47.37 per cent respectively, of Cenvat credit availed by the assessees remained unverified. Specifically during 2014-15, 16 ranges out of 38 ranges had not verified the correctness of Cenvat credit availed by the assessees to the extent of 90 per cent of the credit availed by them. Further, we also noticed that most of the selected ranges as pointed out in paragraph 3.2.2 of this report had not conducted detailed scrutiny of returns and Cenvat verification was being carried for selected units by internal audit of the department. As a result a large portion of Cenvat credit which the assessees used for payment of duty/tax was not verified.

When we pointed this out (between April and July 2015), the Ministry stated (February 2016) that the action has already been initiated.

Two cases are illustrated below:-

3.3.1 We observed in Bettiah central excise and service tax range in Patna Commissionerate that neither internal audit nor detailed scrutiny of returns of M/s. HPCL Biofuels, Lauria was carried out by the department during the period of review. Consequently, Cenvat credit of ₹ 8.09 crore availed by the assessee during the aforesaid period could not be verified from the source documents like input, capital goods and input service invoices and the department completely relied upon the information provided by the assessee in its return defeating the very purpose of compliance verification mechanism of detailed scrutiny and internal audit.

When we pointed this out (June 2015), the Ministry stated (February 2016) that the assessee has been selected for audit for the period for 2015-16.

⁸ Only 38, 40 and 38 ranges out of total 129 selected ranges furnished the data for 2012-13, 2013-14 and 2014-15 respectively.

3.3.2 Similarly, in Mumbai-VII ST Commissionerate, we observed that Cenvat credit amounting to ₹ 2,835.80 crore availed and utilised by M/s. Reliance Communication Ltd., during the period of review remained unverified by the department as the department did not conduct internal audit of the unit for the period 2010-11 to 2014-15 despite the unit being one of the top service tax paying units and falling under mandatory category for internal audit. During our audit we observed non-reversal of Cenvat credit of ₹ 24.36 crore as detailed in Para 4.2.1.

When we pointed this out (June 2015), the Ministry stated (February 2016) that the assessee will be selected for internal audit in future.

During the exit conference, the Ministry stated that due to manpower constraints there is skewed coverage of internal audit and detailed scrutiny.

While acknowledging man power constraints, audit is unable to appreciate how such cases were left out from the 2,183 number of assessees paying more than ₹ three crore covered by internal audit during 2014-15.

Audit is of the view that there is a need for department to revisit the parameters for selection of cases for internal audit/detailed scrutiny keeping the existing man power constraints in view.

Chapter 4: Efficiency of department in ensuring compliance

After introduction of self assessment of duty/tax by the assessee, the department has to ensure compliance verification of duty/tax payment through the tool of scrutiny and internal audit. Audit observed that no detailed scrutiny was carried out by the department. Furthermore non-coverage of mandatory units for internal audit was also observed. Due to non-observance of the compliance verification mechanism as envisaged, we noticed various shortcomings while examining adherence to the rules and regulations of Cenvat Credit Rules, 2004. Some of the cases observed are illustrated below.

4.1 Cenvat credit on inputs and input services

Inputs and input service have been defined under rule 2(k) and 2(l) of Cenvat Credit Rules, 2004.

As per rule 3 ibid, a manufacturer or provider of output service is allowed to avail credit of duties/service tax specified therein which are paid on capital goods/inputs/input service.

Irregular availing and utilisation of Cenvat credit is recoverable along with interest and penalty in terms of rule 14 and rule 15A of Cenvat Credit Rules, 2004.

During scrutiny of the records of 2012-13 to 2014-15, we observed in 83 cases that Cenvat credit of ₹ 62.13 crore was availed on ineligible inputs/input services.

Some of the cases are illustrated below:-

4.1.1 *Cenvat credit availed on ineligible input services*

Rule 2(l) of Cenvat Credit Rules, 2004, defines input service, inter alia, as any service used by a 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 viz., modernisation, renovation etc., but excludes (A) service portion in the execution of a works contract and construction services including service listed under clause (b) of Section 66E of the Finance Act in so far as they are used for (a) construction or 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 except for the provision of one or more of the specified services.

M/s. Jindal Steel and Power Ltd., in Bhubaneswar-II Commissionerate, has availed and utilised input service credit of ₹ 36.67 crore during the period of

review, for setting up of plant and for project work and services related to civil works viz., excavation for foundation, earth work etc., which are excluded from the definition of input services. This resulted in irregular availing and utilisation of Cenvat credit of ₹ 36.67 crore.

When we pointed this out (July 2015), the Ministry admitted the observation (February 2016).

4.1.2 Cenvat credit of input services for the period not covered by notification

According to notification dated 20 June 2012 effective from 1 July 2012, in respect of construction of a complex, building, civil structure or part thereof, intended for a sale to a buyer, Cenvat credit is available in respect of input services and capital goods only. No Cenvat credit is available on inputs used for providing the taxable services. Thus, Cenvat credit on such services provided upto 30 June 2012 was therefore not available.

M/s. AGC Realty Private Ltd., in Delhi ST Commissionerate, availed and utilised Cenvat credit on service tax paid on input services received prior to July 2012 in connection with its output service of construction of residential projects. Since, the services were consumed or received before July 2012 Cenvat credit was not admissible to the service provider. This resulted in inadmissible availing and utilisation of Cenvat credit of ₹ 91.07 lakh.

When we pointed this out (June 2015), the Ministry while admitting the objection intimated (February 2016) that SCN has been issued.

4.1.3 Cenvat credit availed on sales commission

As per rule 2(l) of Cenvat Credit Rules, 2004, sales promotion is an eligible credit, however sales commission is not included in the definition of input service. In the case of M/s. Cadila Healthcare Ltd., {2013(30)STR 3(Guj.)} it was held that the service rendered by the commission agents not being analogous to the activities mentioned in the definition, would not fall within the ambit of the expression activities relating to business or sales promotion. Consequently, Cenvat credit would not be admissible in respect of the commission paid to commission agents. Appeal in the case of M/s. Cadila Healthcare Ltd., was filed before the Hon'ble Supreme Court and the Apex Court had seized the matter and no stay order was granted in that case {2014 (34) S.T.R. 814 (Guj.)}.

M/s. Ballavpur Paper Manufacturing Ltd., in Bolpur Commissionerate, cleared kraft paper through various selling agents and paid commission on sale along with applicable service tax. The assessee then availed of credit of service tax so paid which was irregular. This resulted in irregular availing of Cenvat credit of ₹ 1.40 crore on sales commission during the period of review.

When we pointed this out (September 2014) the Ministry stated (February 2016) that the credit availed by the assessee was regular in the light of circular dated 29 April 2011 and the judgement of Gujarat High Court was not binding on the assessee.

The reply of the Ministry is not acceptable since if there is any conflict between jurisdictional High Court and Board's circular, the decision of jurisdictional High Court is binding to the department rather than its circular {2014 (34) S.T.R. 814 (Guj.)}.

4.1.4 Cenvat credit availed on exempted goods

Rules 6(4) and 6(1) of Cenvat Credit Rules, 2004, envisage that no Cenvat credit shall be allowed on capital goods or input service which are used exclusively for the manufacture of exempted goods or for providing exempted service.

M/s. Travancore Cochin Chemicals Ltd., in Kochi Commissionerate, established an Ammonium Per-chlorate Experimental Plant for ₹ 24 crore, exclusively for producing Sodium Chlorate crystal with the support of M/s. Vikram Sarabai Space Centre (VSSC). The finished goods were supplied to M/s. VSSC under exemption notification dated 1 March 1997. During scrutiny it was noticed that the assessee availed Cenvat credit on capital goods of ₹ 63.60 lakh on input services of ₹ 28.02 lakh used for the above plant which was not correct. This resulted in irregular availing of Cenvat credit of ₹ 91.62 lakh during the period of review.

When we pointed this out (July 2015), the Ministry stated (February 2016) that since the capital goods in question were used for manufacture of both dutiable and exempted goods rule 6(4) of Cenvat Credit Rules, 2004 is not attracted in this case.

The reply of the Ministry is not acceptable as it was observed in audit that there was no clearance of dutiable goods.

4.1.5 Cenvat credit of countervailing duty wrongly paid

As per explanation given under sub-section (1) of Section 5A of the Central Excise Act, 1944, where an exemption under sub-section (1) in respect of any excisable goods from the whole of the duty of excise leviable thereon has been granted absolutely, the manufacturer of such excisable goods shall not pay the duty of excise on such goods.

Further, as per rule 2(d) of the Cenvat Credit Rules, 2004, exempted goods means, excisable goods which are exempt from the whole of the duty of excise leviable thereon, and include goods which are chargeable to "Nil" rate of duty.

The Board in its circular dated 14 January 2011, clarified that- “if the assessee pays any amount as excise duty on exempted goods, the same cannot be allowed as Cenvat credit to the downstream units, as the amount paid cannot be treated as duty of excise under rule 3 of Cenvat Credit Rules, 2004”.

M/s. Jindal Steel and Power Ltd. and M/s. Ganesh Sponge Pvt. Ltd., in Bhubaneswar-II Commissionerate, availed Cenvat credit on imported coal on which CVD at the rate of two percent was paid. As the said goods falls under the category of exempted goods as per the rule cited supra, availing of credit on the same was irregular. This resulted in irregular availing of Cenvat credit of ₹ 3.50 crore (₹ 3.38 crore + 0.12 crore) during the period 2013-14 to 2014-15.

When we pointed this out (July 2015), the Ministry while admitting the observation stated (February 2016) that SCNs are being issued.

4.2 Reversal of Cenvat credit

As per rule 6(2) of Cenvat Credit Rules, 2004, where an assessee deals with both dutiable and exempted manufacture/service he shall maintain separate account of receipt, consumption and inventory of input/input services intended for use in dutiable manufacture/service and those intended for use in exempted manufacture/service and take credit of only the former portion. Further, the manufacturer of goods or the provider of output services, opting not to maintain separate accounts, shall pay an amount equal to six per cent of the value of the exempted good and exempted services or pay an amount as determined under sub-rule (3A) ibid.

During scrutiny of records we observed 18 cases in 12 Commissionerates, the assessees either had not paid or short paid the amount of ₹ 32.74 crore payable under rule 6 of Cenvat Credit Rules, 2004, during the period of review. A few cases are illustrated below:-

4.2.1 Section 64 of Chapter V of Finance Act, 1994, excludes the applicability of service tax in the State of Jammu and Kashmir. Since service tax is not payable in respect of services provided in Jammu and Kashmir, Cenvat credit of the related input services is not admissible. 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 66 of the Finance Act, 1994.

M/s. Reliance Communications Ltd., in Mumbai-VII ST Commissionerate, was engaged in providing taxable, exempted and non-taxable telecommunication services. Scrutiny of records for the period of review revealed that assessee had provided non-taxable services to Jammu and Kashmir clients and earned

income of ₹ 222.27 crore. The assessee did not maintain separate accounts for input services used in the provision of taxable and non-taxable services. Further, no amount was paid as per rule 6(3A) against the non taxable services related to Jammu and Kashmir. This resulted in non-payment of ₹ 24.36 crore for years 2013-14 and 2014-15.

When we pointed this out (July 2015), the Ministry intimated (February 2016) that an SCN is being issued.

4.2.2 M/s. Rashtriya Chemical and Fertilisers Ltd., Thal, in Mumbai LTU Commissionerate, was engaged in the manufacture of dutiable and exempted products. The assessee has two manufacturing units at Trombay and Thal. Scrutiny of records of Thal unit for the years 2012-13 and 2013-14 revealed that, assessee had availed proportionate service tax credit on common input services which were received exclusively for the Thal unit for removal of dutiable goods and for provision of taxable services. While reversing the amount under rule 6(3) the assessee had considered the turnover ratio of the entire company (both units) which was not correct as the turnover ratio of Thal Unit alone was required to be considered. This resulted in excess availing of Cenvat credit ₹ 5.29 crore.

When we pointed this out (April 2015), the Ministry while admitting the observation intimated (February 2016) that the SCN is being issued.

4.2.3 As per rule 6(3B) of Cenvat Credit Rules, 2004, a banking company and a financial institution including a non-banking finance company (engaged in providing services by way of extending deposits, loans or advances) shall pay for every month equal to fifty per cent of the Cenvat credit availed on inputs and input services in that month with effect from 1 April 2011.

During scrutiny of records of M/s. Federal Bank Ltd., in Kochi Commissionerate, we observed that the assessee availed Cenvat credit of input services amounting to ₹ 32.83 crore during the year 2012-13 but reversed only ₹ 15.76 crore instead of ₹ 16.42 crore. This resulted in short reversal of ₹ 65.57 lakh.

When we pointed this out (March 2014) the Ministry intimated (February 2016) the reversal of Cenvat credit of ₹ 65.57 lakh along with interest of ₹ 19.75 lakh.

4.2.4 M/s. Jindal Steel and Power Ltd., in Bhubaneswar-II Commissionerate has cleared two exempted products viz., calcined lime and sulphur valuing ₹ 9.11 crore during the period 2013-14 and 2014-15 without payment of duty. However, the assessee had availed Cenvat credit on inputs viz. imported lime stone and imported quick lime lumps and input services viz., manpower agency services, goods transport agency on transportation of coal and other

input services. Since the assessee had not maintained separate accounts, as per rule 6(3) he is liable to pay an amount of ₹ 54.64 lakh.

When we pointed this out (July 2015), the Ministry while admitting the observation stated (February 2016) that the SCN is under process.

4.2.5 M/s. West Bengal Electronics Industry Development Corporation Ltd., in Kolkata-I ST Commissionerate, rendered various taxable and exempted services during the period of review. The assessee, however, did not exercise any option under rule 6 ibid for not maintaining separate accounts for common input services used for both taxable services and exempted service. Since the assessee had not maintained separate accounts, as per rule 6(3) he is liable to pay an amount of ₹ 37.36 lakh.

When we pointed this out (May 2015), the Ministry admitted the audit observation (February 2016).

4.3 Excess availing of Cenvat credit

Rule 3 of Cenvat Credit Rules, 2004, provides that a manufacturer/service provider shall be allowed to take Cenvat credit of duties specified therein paid on inputs, capital goods and input service received for use in or in relation to manufacturer of final products or provision of output service, on the basis of documents specified in rule 9 ibid.

During scrutiny of records we observed 22 cases, in 12 Commissionerates, availing of Cenvat credit was in excess of the admissible amount, which resulted in irregular availing of Cenvat credit of ₹ 20.20 crore during the period from 2012-13 to 2014-15. A few cases are illustrated below:-

4.3.1 M/s. Jindal Steel and Power Ltd., Angul in Bhubaneswar-II Commissionerate, has availed input credit of countervailing duty (CVD) and special additional duty (SAD) of ₹ 47.95 crore in August 2014, against the apportioned entitlement of ₹ 29.90 crore. The excess availing of credit is on account of credit pertaining to the other unit at Raigarh. This resulted in excess availing of credit of ₹ 18.05 crore.

When we pointed this out (April 2015), the Ministry while admitting the observation intimated (February 2016) that the SCN is being issued.

4.3.2 On audit examination of ER-1/Cenvat credit records of M/s. Pricol Ltd., in Pune-III Commissionerate, revealed that in the ER-1 returns, the service tax credit amount was taken both in input credit column as well as in service tax credit column in the month of May, June, October and November 2014. This resulted in double availing of Cenvat credit of service tax of ₹ 25.15 lakh.

When we pointed this out (June 2015), the Ministry intimated (February 2016) the recovery of ₹ 25.15 lakh along with interest and penalty of ₹ 5.48 lakh.

4.4 Irregular availing of Cenvat credit

4.4.1 On ineligible documents

Rule 9 of Cenvat Credit Rules, 2004, specifies the documents on the basis of which a manufacturer/service provider is allowed Cenvat credit of duty/service tax paid on input/capital goods or input service, which inter alia includes an invoice, bill of entry etc.

During scrutiny of records we observed 18 cases, in 10 Commissionerates, that Cenvat credit was availed on ineligible documents. This resulted in irregular availing of Cenvat credit of ₹ 2.36 crore during the period of review. A few cases are illustrated below:-

Scrutiny of records of M/s. BBM Accoustic India Pvt. Ltd., in Pune-III Commissionerate, revealed that the assessee availed Cenvat credit of ₹ 62.71 lakh on the basis of service tax payment challan copy of subsidiary company which is not correct. This resulted in irregular availing of Cenvat credit of ₹ 62.71 lakh.

When we pointed this out (June 2015), the Ministry while not admitting the observation stated (February 2016) that as per circular dated 30 April 2010 in case of 'Associated enterprises' credit of service tax can be availed when the payment has been made to the service provider.

The reply of the Ministry is silent on audit observation related to availment of credit on the copy of challan of subsidiary company which is inadmissible.

4.4.2 Cenvat credit on old invoices

Rule 4 of Cenvat Credit Rules, 2004, with effect from 1 September 2014, was amended to provide, inter alia, that Cenvat credit shall not be allowed after six months of the date of documents issued under rule 9, ibid.

During scrutiny of records we observed 14 cases in seven Commissionerates, that Cenvat credit of ₹ 2.83 crore was availed on invoices/documents which were older than six months. A few cases are illustrated below:-

4.4.2.1 M/s. Coca Cola India Pvt. Ltd., in Pune-III Commissionerate, availed credit of duty paid on inputs on the basis of invoices/documents which were older than six months between September 2014 and March 2015. This resulted in irregular availing Cenvat credit of ₹ 73.86 lakh.

When we pointed this out (June 2015), the Ministry intimated (February 2016) that an SCN was issued to assessee.

4.4.2.2 M/s. Ford India Pvt. Ltd., in Chennai LTU Commissionerate, availed Cenvat credit in November 2014 based on the invoices which were more than six months old. This resulted in irregular availing of Cenvat credit of ₹ 49.65 lakh.

When we pointed this out (June 2015), the Ministry stated (February 2016) that the credit availed against the invoices were in order as the time limit was extended to one year vide notification dated 1 March 2015.

The reply of the Ministry is not acceptable since the notification dated 1 March 2015 is effective from 1 March 2015 only.

Recommendation No.5

The government may consider inserting provision for furnishing detailed information regarding Cenvat credit availed by the assessee containing invoices/documents nos., date of invoices, name of goods with chapter heading, amount of credit taken etc. so that preliminary check may be exercised at Range level.

The Ministry intimated (February 2016) that the recommendation is under examination.

4.5 Self adjustment of Cenvat credit

A duty of excise/tax paid in excess shall be claimed as refund under Section 11B of the Central Excise Act, 1944. Therefore, any suo-moto adjustment of duty, once paid, shall lead to non-payment of duty and an assessee may get the excess duty paid earlier only by claiming refund from the department.

4.5.1 M/s. Vodafone Cellular Ltd., in Kochi Commissionerate, engaged in providing telecommunication and business support services, paid service tax based on the invoices issued by them as per rule 4A of the rules, ibid. However, while discharging their service tax liability during 2012-13 to 2014-15, the assessee adjusted ₹ 2.41 crore on account of excess service tax paid in earlier months by taking credit under the said rule. On further examination, we observed that whenever sales return transactions of pre-paid coupons and non-receipt of amounts of post-paid connections were noticed, corresponding service tax paid at the time of raising invoices were adjusted in current months service tax liability. Since, such adjustment can be done only when the assessee has refunded the payment received including service tax or issued a credit note for the same which was not the case in the instant observation, the adjustment made by the assessee was held to be irregular. This resulted in irregular availing and utilisation of credit of ₹ 2.41 crore.

When we pointed this out (June 2015), the Ministry intimated (February 2016) that an SCN is being issued.

4.5.2 Scrutiny of records of M/s. Titagarh Wagon Ltd., in Kolkata LTU Commissionerate, revealed that the assessee had raised an invoice to M/s. GATX India (P) Ltd. for 'Bogie Container Flat' on 31 December 2014, but the said goods were not actually cleared on that date. The goods were actually cleared on January 2015 and a separate invoice dated 28 January 2015 was again issued to M/s. GATX India Pvt. Ltd. The invoice raised by M/s. Titagarh Wagon Ltd. during December 2014 was then returned by M/s. GATX India Pvt. Ltd. and assessee availed suo-moto credit on the basis of this invoice. This resulted in irregular availing of Cenvat credit of ₹ 65.73 lakh during 2014-15.

Similarly, M/s. Prabhat Zarda Factory (India) Pvt. Ltd., in Noida Commissionerate availed suo-moto Cenvat credit of ₹ 3.20 lakh during 2012-13.

When we pointed this out (between May and June 2015) the Ministry intimated (February 2016) the recovery of ₹ 65.73 lakh in respect of M/s. Titagarh Wagon Ltd. The Ministry in the case of M/s Prabhat Zarda Factory (India) Pvt. Ltd. stated that the assesee was not eligible to take cenvat credit.

4.6 Availing of Cenvat credit without making payment

Sub-rule 7 of rule 4 of Cenvat Credit Rules, 2004, the Cenvat credit in respect of input service shall be allowed, on or after the day on which the invoice, bill or, as the case may be, challan referred to in rule 9 is received. Further, proviso to the said rule provides that in case the payment of the value of input service and service tax paid or payable as indicated in the invoice/bill is not paid within three months of the date of the invoice/bill, the service provider who has taken credit on such input service shall pay an amount equivalent to the Cenvat credit availed on such input service.

Further, this rule provides that if any payment or part thereof, made towards an input service is refunded or credit note is received by the manufacturer or the service provider who has taken credit on such input services, he shall pay an amount equal to the Cenvat credit availed in respect of the amount so refunded or credited.

During scrutiny of records we observed two cases in Delhi-I ST Commissionerate, the service providers availed Cenvat credit on input services in violation of above rule either by not making payment of value of input service along with service tax payable thereon within the prescribed time limit of three months or making delayed payment of the same. This

resulted in irregular availing of Cenvat credit of ₹ 1.49 crore during the period of review.

A case is illustrated below:-

Scrutiny of records of M/s. Saum Infra Pvt. Ltd., in Delhi-I ST Commissionerate, revealed that the assessee had availed and utilised Cenvat credit of ₹ 1.48 crore on input services in respect of which the assessee had not paid the value of input service till the date of audit (June 2015). This resulted in irregular availing of Cenvat credit of ₹ 1.48 crore during the period 2012-13 to 2013-14.

When we pointed this out (June 2015) the Ministry intimated (February 2016) the recovery of ₹ 2.34 crore.

4.7 Distribution of Cenvat credit by Input Service Distributor (ISD)

As per rule 2 (m) of Cenvat Credit Rules, 2004, “input service distributor” means an office of the manufacturer or producer of final products or provider of output service, which receives invoices issued under rule 4A of the Service Tax Rules, 1994, towards purchases of input services and issues invoice, bill or, as the case may be, challan for the purposes of distributing the credit of service tax paid on the said services to such manufacturer or producer or provider, as the case may be. Rule 7 of Cenvat Credit Rules, 2004, prescribes the conditions for distribution of Cenvat credit by an input service distributor. One of the conditions is that the credit of service tax attributable to service used by one or more units exclusively engaged in manufacture of exempted goods or providing of exempted services shall not be distributed. Further, the credit of service tax attributable to service used by more than one unit shall be distributed pro rata on the basis of the turnover of such units during the relevant period to the total turnover of all its units, which were operational in that year.

During scrutiny of records we observed six cases in six Commissionerates credit of ₹ 1.05 crore was irregularly distributed and/or availed during the period 2012-13 to 2014-15. Two cases are illustrated below:-

M/s. Alok Industries, in Silvassa Commissionerate, is having five sister units (one situated at Vapi, three situated at Silvassa and one situated at Navi Mumbai). However, the assessee availed and utilised Cenvat credit in respect of input services of common nature viz. consulting fees, profession fees for arranging funds, SAP maintenance, etc. All these services are of common nature and pertain to M/s. Alok Industries Ltd., as a whole and not only to the assessee unit at Silvassa. Hence, availing of Cenvat credit of ₹ 64.64 lakh of common input services at one unit was irregular.

When we pointed this out (June 2015) the Ministry intimated (February 2016) the recovery of amount of ₹ 64.64 lakh.

4.8 Transfer of Cenvat credit

Rule 12A of Cenvat Credit Rules, 2004, defines the procedure and facilities for large tax payers who have registered under LTU. As per rule 12A(4) of the Cenvat Credit Rules, 2004, as amended from time to time , a large tax payer may transfer, Cenvat credit taken, on or before the 10 July 2014 by one of its registered manufacturing premises or premises providing taxable service to his other such registered premises subject to certain conditions.

M/s. Supreme Industries Ltd. (Silvasa Unit), in Mumbai LTU Commissionerate, availed and utilised the Cenvat credit of ₹ 60 lakh in 2014-15 on the basis of the transfer of credit by Halol Unit on 31 July 2014. Scrutiny of records of transferor unit (Halol unit) revealed that the credit of ₹ 10.17 lakh availed by it during the period from 11 July 2014 to 31 July 2014 was also transferred to Silvasa Unit. Thus, the amount of Cenvat credit transferred in excess to the balance of Cenvat credit as on 10 July 2014 by the transferor unit was not correct. This resulted in irregular availing and utilisation of Cenvat credit of ₹ 10.17 lakh by Silvasa Unit.

When we pointed this out (June 2015) the Ministry intimated (February 2016) the recovery of ₹ 10.17 lakh along with interest of ₹ 1.83 lakh.

4.9 Cenvat credit of fully/partially written off inputs or capital goods

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 off fully or partially has been made in the books of account, then the manufacturer or service provider shall pay an amount equivalent to the Cenvat credit taken in respect of the said inputs or capital goods.

During scrutiny of records we observed four cases, in four Commissionerates, that value of inputs/capital goods, on which Cenvat credit was availed of, was either written off or provision for write off was made in the books of accounts before the same being put to use but corresponding Cenvat credit was not reversed. This resulted in non-reversal of Cenvat credit of ₹ 44.81 lakh during the period of review. A case is illustrated below: -

M/s Innovative Technomics Pvt. Ltd., in Pune-III Commissionerate, had discarded stock of ₹ 2.19 crore during the year 2012-13. Audit observed that though the Cenvat credit was availed on such stock, an amount equivalent to

Cenvat credit availed was not reversed by the assessee at the time of discarding of stocks. This resulted in irregular credit of ₹ 22.57 lakh.

When we pointed this out (June 2015), the Ministry while admitting the observation stated (February 2016) that the SCN is being issued.

4.10 Cenvat credit of education cess and secondary higher education cess wrongly paid

A manufacturer or producer of final products or a provider of output service is allowed to take Cenvat credit of all duties, taxes and cesses enlisted in rule 3(1) of Cenvat Credit Rules, 2004. After exemption of the education cess and the secondary and higher education cess on countervailing duty (CVD) vide Customs notifications dated 17 March 2012 availing of Cenvat credit of above cesses either in full or proportionate to the CVD will be irregular as cesses paid on the Custom is not included in rule 3(1) above.

During scrutiny of records we observed in 17 cases in 12 Commissionerates that assessees have taken credit of cesses paid on custom duty which resulted in irregular availing of Cenvat credit of ₹ 85.61 lakh during the period of review. A case is illustrated below:-

M/s. Concast Bengal Industries Ltd., in Bolpur Commissionerate, availed and utilised credit of education cess and secondary and higher education cess of ₹ 32.00 lakh paid on custom duty on the basis of bill of entry pertaining to imported inputs. This resulted in irregular availing of Cenvat credit of ₹ 32.00 lakh during the period of review.

When we pointed this out (September 2014), the Ministry while admitting the observation (February 2016) stated that the SCN is being issued.

4.11 Use of Cenvat credit for payment of service tax under reverse charge

As per explanation given below rule 3(4) of Cenvat Credit Rules, 2004, Cenvat credit cannot be used for payment of service tax in respect of services where the person liable to pay tax is the service recipient.

During scrutiny of records we observed three cases in three Commissionerates, wherein service tax was paid as recipient of service by utilizing Cenvat credit account. This resulted in irregular utilisation of Cenvat credit of ₹ 11.34 lakh during the period of review. A case is illustrated below:-

M/s. Ascent Buildtech Pvt. Ltd., in Delhi-I ST Commissionerate paid service tax of ₹ 4.50 lakh on input services under reverse charge mechanism as service recipient by utilizing Cenvat credit. This resulted in irregular utilisation of Cenvat credit of ₹ 4.50 lakh during the period of review.

When we pointed this out (June 2015) the Ministry intimated (February 2016) that the assessee deposited the amount.

4.12 Removal of capital goods after being used

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

During scrutiny of records we observed four cases in three Commissionerates, that an amount of ₹ 13.30 lakh was not reversed upon removal of used capital goods during the period of review.

M/s Suvi International Pvt. Ltd. in Delhi-I Commissionerate had availed and utilised Cenvat credit of ₹ 30.04 lakh on the capital goods. The assessee later on sold these capital goods as waste and scrap. However, the proportionate Cenvat credit of ₹ 8.12 lakh had not been reversed.

When we pointed this out (June 2015), the Ministry stated (February 2016) that no dues are pending against the assessee.

The reply of the Ministry is silent on the aspect of the reversal of Cenvat credit or payment of duty on transaction value on selling of capital goods as waste and scrap.

4.13 Non-reversal of Cenvat credit on goods sent to job worker

Rule 4 (5a) of the Cenvat Credit Rules, 2004, if the inputs or capital goods, sent to a job worker for further processing, testing, repair etc. are not received back in the factory within one hundred and eighty days of their being sent to a job worker, the manufacturer or provider of output service shall pay an amount equivalent to the Cenvat credit attributable to the inputs or capital goods by debiting the Cenvat credit or otherwise.

Scrutiny of records of M/s. LanXESS India Pvt. Ltd., M/s. Nuberg Engineering Ltd., and M/s. Rahul Ferromet and Engineering Pvt. Ltd., in Bharuch Commissionerate, revealed that the inputs or capital goods, sent to a job worker for further processing, testing, repair etc. were not received back in the factory within one hundred and eighty days, but the manufacturer or provider of output service failed to reverse the credit attributable to inputs/capital goods not received or short received. This resulted in non-

reversal of Cenvat credit of ₹ 23.42 lakh ($20.11 + 2.13 + 1.18$) during the period of review.

When we pointed this out (June 2015) the Ministry intimated (February 2016) the reversal of Cenvat credit of ₹ 23.42 lakh.

4.14 Simultaneous availing of Cenvat credit and depreciation

As per rule 4(4) of Cenvat Credit Rules, 2004, the Cenvat credit in respect of capital goods shall not be allowed in respect of that part of the value of capital goods which represents the amount of duty on such capital goods, which the manufacturer or provider of output service claims as depreciation under Section 32 of the Income Tax Act, 1961.

M/s. Shubham Starch Chemicals Pvt. Ltd., in Faridabad-II Commissionerate, availed Cenvat credit of ₹ 2.95 lakh (including cess) on the capital goods during the year 2013-14 but also capitalised the whole amount including excise duty element on which the depreciation was claimed as per Section 32 of the Income Tax Act 1961. It resulted in irregular availing of Cenvat credit of ₹ 2.95 lakh.

When we pointed this out (July 2015), the Ministry while admitting the observation intimated (February 2016) the reversal of Cenvat credit of ₹ 2.95 lakh along with interest.

Similarly, M/s. Steelfab Building Systems, in Silvassa Commissionerate, irregularly availed Cenvat credit of ₹ 2.01 lakh during 2014-15.

When we pointed this out (April 2015), the Ministry while admitting the observation intimated (February 2016) the reversal of Cenvat credit of ₹ 2.01 lakh along with interest of ₹ 0.53 lakh.

4.15 Other issues

During scrutiny of records we observed in seven cases Cenvat credit was irregularly availed/utilised in violation of provision/notification involving revenue of ₹ 48.28 lakh. These cases are tabulated below: -

Sl. No.	Name of assessee	Commissionerate	Period	Revenue involved ₹ in lakh)
1.	M/S. Icon Household Product (P) Ltd.	Guwahati	2013-15	11.28
2.	M/s. R.P. Multimetals Private Ltd.	Chandigarh-I	2014-15	1.51
3.	M/s. Bubna Advertising	Delhi-I ST	2012-14	9.54
4.	M/s. Overseas Logistics Pvt. Ltd.	Delhi-I ST	2012-14	8.80
5.	M/s. Arihant Video Communication	Delhi-I ST	2013-15	3.66
6.	M/s. Suvi international Pvt. Ltd.	Delhi-I	2014-15	1.40
7.	M/s. Uttam (Bharat) Electricals Private Ltd., Unit-II, Jaipur	Jaipur	2012-15	12.09
	Total			48.28

When we pointed this out (between April and June 2015), the Ministry while admitting the observation in all cases intimated (February 2016) the recovery in six cases except for M/s. Uttam Electricals Pvt. Ltd.

4.16 Conclusion

Excessive use of Cenvat credit to the extent of seven to ten times of national average in service tax and seven times in central excise in some of selected Commissionerates could indicate the likelihood of misuse of Cenvat credit by assessees. Moreover, around 90 per cent of Cenvat credit availed was not verified by the department through detailed scrutiny and internal audit in 16 ranges.

In view of the large amount of duty being paid through Cenvat credit, Audit is of the opinion that the department needs to strengthen its internal control mechanism using the existing man power judiciously.

New Delhi

Dated: 03 May 2016



(SANJEEV GOYAL)

Principal Director (Central Excise)

Countersigned



New Delhi

Dated: 03 May 2016

(SHASHI KANT SHARMA)

Comptroller and Auditor General of India

Abbreviations

ACES	Automation of Central Excise and Service Tax
CAG	Comptroller and Auditor General of India
CBEC	Central Board of Excise and Customs
CDR	Commissionerate, division and range
CE	Central Excise
Cenvat	Central Value Added Tax
CVD	Countervailing duty
ER	Excise Return
GST	Goods and Service Tax
Ltd.	Limited
LTU	Large taxpayer unit
Modvat	Modified Value Added Tax
PLA	Personal Ledger Account
Pvt.	Private
SCN	Show Cause Notice
SSI	Small Scale Industry
ST	Service Tax
TRU	Tax Research Unit
VSSC	Vikram Sarabai Space Centre

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