

CENVAT CREDIT UNDER SERVICE TAX AND EXCISE

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1. Preamble:

Excise Duty and Service Tax are Central Government levy. Both are destination based consumption tax, incidence of which is passed on to ultimate consumers. These are major indirect taxes which operate on value added scheme of taxation (VAT system). Under VAT system, each person in transaction chain is taxed on the value addition done by him. The concept of taxing value addition is achieved by granting credit of input tax or duties to manufacturer / service provider through Cenvat Credit Scheme. This scheme integrates Central Government indirect taxes viz. Excise Duty and Service Tax. The Cenvat credit scheme operates through Cenvat Credit Rules, 2004 (hereinafter referred to as “CCR”).

This article deals with current provisions only. For the sake of brevity, scope of article is restricted to substantive provisions of Cenvat Credit Rules, 2004. Article does not deal with provisions pertaining to procedures, penalty and interest. The purpose of this article is to elucidate basic concepts relating to CCR in simple and lucid manner and hence author has refrained from reproduction of sections, rules and clauses etc in this article.

2. Historical back ground:

2.1. Manufacturers:

Period	Relevant Scheme / Rules	Assessee's entitlement
01.03.1986 to 28.02.1994	Modvat Scheme	Credit for duties paid on inputs only.
01.03.1994 to 09.09.2004	Modvat Scheme	Credit for duties paid on inputs. Credit for duties paid on capital goods.
10.09.2004 onwards	Cenvat Credit Rules, 2004	Credit for duties paid on inputs. Credit for duties paid on capital goods. Credit for service tax on input services.

2.2. Service Providers:

Period	Relevant Scheme / Rules	Assessee's entitlement
01.07.1994 to 15.08.2002	----	No credit for input service tax.
16.08.2002 to 14.05.2003	Service Tax Credit Rules, 02	Credit for service tax paid on input services falling in same category.
15.05.2003 to 09.09.2004	Service Tax Credit Rules, 02	Credit for service tax paid on all input services used for providing out put services.
10.09.2004 onwards	Cenvat Credit Rules, 2004	Credit for duties paid on all input goods. Credit for duties paid on capital goods. Credit for service tax paid on all input services.

3. Extent and commencement of present Cenvat Scheme:

Cenvat Credit Rules, 2004 is introduced w.e.f. 10.09.2004 vide Notification No.23/2004-Central Excise (N.T.) dated 10.09.2004. This is a unique Rule which is common for Excise and Service Tax legislation. The input tax credit mechanism under both these legislations is governed by this Rule. CCR extends to whole of India with some exception for Jammu and Kashmir. Service tax is not applicable to Jammu & Kashmir. Proviso to Rule 1(2) of CCR, therefore, provides for non-applicability of these Rules to service tax. Cenvat implications in Jammu & Kashmir (J&K) are as under:

- Manufacturer in J&K is entitled for Cenvat credit of duty on inputs and capital goods. However he is not eligible to claim Cenvat credit of service tax, if any, paid on input services.
- Service provider in J&K is not entitled to Cenvat credit of duty / tax on inputs, capital goods and input services.

4. Basic Objectives of Cenvat Credit Mechanism:

- 4.1. To avoid or minimize cascading effect of indirect taxes.
- 4.2. To minimize tax incidence on ultimate consumer of goods / services.
- 4.3. To ensure levy of tax on value addition by respective assessee.
- 4.4. To eliminate or minimize possibilities of levy of tax on tax.

Following table helps readers in understanding how Cenvat scheme achieves its objectives:

Tax Scenario - Pre and Post Cenvat:

Cost break up	Basic Cost	Tax Element	Total Cost	Remark
Raw Material	1,00,000	8,240	1,08,240	Excise rate 8.24%
Taxable Services availed	50,000	5,150	55,150	Service tax 10.30%
Overheads (Not liable to ST)	25,000	---	25,000	
Profit markup	20,000		20,000	
Total	1,95,000	13,390	2,08,390	
Excise duty on finished goods	16,068	17,171	17,171	@ 8.24%
Sales price	2,11,068	30,561	2,25,561	Pre-Cenvat price
<u>Less</u> : Cenvat (Input Tax)		(13,390)	(13,390)	
Excise duty on tax element of Rs.13,190.		(1,103)	(1,103)	
Sales price (Post-Cenvat)	2,11,068	16,068	2,11,068	

5. Underlying philosophy of scheme:

Cenvat scheme is based on mutual trust. Entire scheme can be visualized as self maintained duty entitlement / utilization passbook by the manufacturer / service provider. The revenue authorities usually rely on the records of assessee. It is, therefore, incumbent on assessees to be conservative and cautious while availing benefits under Cenvat Scheme. The deterrent provisions for levy of interest and penalties are prescribed for wrong availment and utilization of Cenvat credit.

6. Concept of availment and utilization:

Availment of input tax credit and utilization of accumulated tax credits are important aspects of the scheme. Many people feel that availment and utilization is one and the same. However, both are different from each other as explained under:

- Availment refers to assessee's entitlement to claim input tax credit.
- Availment of input tax credit is a first stage of scheme.
- Assessee is entitled to avail tax / duty credit on inputs, capital goods and input services used for providing taxable services or manufacture of dutiable goods.
- Availment can be visualized as credit entry in self maintained pass book.

- Utilization means use of Cenvat credit balance for payment of out put tax such as excise duty, service tax, education cess etc.
- Output tax liability can be discharged from accumulated Cenvat. There is no difference between physical cash payment and payment from Cenvat account.
- Utilization can be visualized as debit entry in self-maintained pass book.

7. Nature of Input tax credit:

Material cost, capital cost and overheads are major cost components for any manufacturer or service provider. All these cost components suffer tax incidence in form of excise duty or service tax levied by vendors. CCR uses following terms for cost components suffering input tax incidence.

- Input – Raw materials, consumables and other goods used in manufacture or service provision.
- Capital goods – Assets used for manufacture or service provision.
- Input services – Services used for manufacture or service provision.

Above terms are specifically defined in CCR and it has specific meanings. Same are dealt at length in later part of this article.

8. Persons eligible for Cenvat Credit:

Following persons are eligible for Cenvat Credit under Rule 3(1) of CCR:

- Manufacturer of final products.
- Provider of taxable service.

Term “final product” is defined under Rule 2(h) of CCR to mean excisable goods manufactured or produced from inputs or using input services. Thus the person engaged in the manufacturing activity as defined under Section 2(f) of Excise Act, 1944 can be treated as manufacturer of final products.

Section 65(105) of Finance Act, 1994 lists out the taxable services. The provider of any of such services [except GTA service covered under Section 65(105)(zzp)] is a provider of taxable service.

Above referred persons are entitled to Cenvat credit provided their activities are not exempt under excise or service tax legislation.

9. Person not eligible for Cenvat availment::

Following persons are not eligible for Cenvat availment as they are not manufacturer of excisable goods / provider of taxable services or there are specific provisions restricting Cenvat availment:

- Traders including Importers, Wholesalers, Retailers, Stockiest.
- Manufacturer of non-excisable goods.
- Manufacturer of excisable goods availing small scale exemption under Notification No. 8/2003 is not entitled to Cenvat in respect of input and input services. However, such a manufacturer is eligible for Cenvat in respect of capital goods.
- Job worker claiming excise exemption under Notification No. 214/86.
- Provider of non-taxable or exempt services.
- Service provider claiming threshold exemption under Notification No.8/2008-ST dated 01.03.2008.
- Service provider claiming deduction of value of goods sold / used under Notification No. 12/2003 dated 20.06.2003 is not eligible for Cenvat of excise duty on input goods.
- Goods transport operator as GTA service is excluded from the definition of output service as defined under Rule 2(p) of CCR.
- Service provider providing works contract services and opting for composition scheme is not entitled to Cenvat credit in respect of inputs. However, such a service provider is eligible for Cenvat Credit in respect of capital goods and input services.

Following service providers are entitled to claim abatement under Notification No. 1/2006 dated 01.03.2006:

Mandap Keepers	Tour Operators	Rent-a-Cab Services
Convention Services	Outdoor Catering	Pandal & Shamiana Services
Erection Commissioning or Installation	Commercial or Industrial Construction Service	Construction of Complex
Transportation of Goods in Container by Rail	Job workers for manufacture of cycle, cycle rikshaw, hand operated sewing machine.	Services provided in relation to Chit (Notification No. 27/2008-ST dated 27.05.2008)

If such service provider claims Cenvat, he is not entitled to abatement under the said notification. Even minuscule claim of Cenvat credit will jeopardize the abatement claim. Such service provider should be very cautious in this regard.

10. Eligibility of manufacturer exporter / service exporter to avail Cenvat Credit :

Question is often raised whether manufacture exporter not paying excise duty on clearance of goods or service exporter exporting service without payment of service tax is eligible for Cenvat?

It is clarified by Ministry of Law Advice dated 29.10.1974 that goods cleared for export is a clearance `without payment of duty'. They are not exempt goods. CBE&C Circular No.278/112/96-CX dated 11.12.1996 have also confirmed that exempted goods are those goods which are exempted U/S 5A of Central Excise Act. This can be termed as chargeable to `Nil' rate of duty as in fact goods are dutiable. Thus goods exported under bonds are not exempt goods. This view has been accepted by judiciary in Reliance Industries Ltd Vs CCE 1999 (112) ELT 653 (CEGAT) and many other cases.

Exempted services U/R 2(e) means the services exempt from whole of service tax leviable thereon or services on which no service tax is leviable U/s 66. Export of services is not exempted under any notification. Service tax is leviable U/s 66 of Finance Act on such services. The said services are allowed to be exported without payment of service tax under Rule 4 of Export of Service Rules, 2005. Export of services is not exempted services within the meaning of CCR. This view is confirmed by CBE&C Circular No.868/6/2008-CX dated 09.05.2008.

Even Rule 5 of CCR takes cognizance of this legal position. It entitles manufacturer exporter / service exporter to claim refund of accumulated Cenvat credit balance.

In view of what is stated above, one may safely conclude that manufacturer exporter / service exporter is eligible to avail Cenvat credit in respect of export of excisable goods or export of taxable services.

11. Duties, Taxes, Cess Eligible For Tax Credit:

Rule 3(1) of CCR prescribes following duties, taxes and cess paid on **inputs, capital goods and input services** are eligible for Cenvat Credit.

11.1. Regular / general:

- Excise duty under 1st and 2nd Schedule to Excise Tariff Act.
- Service tax leviable U/s 66 of Finance Act 1994 (Refer Para 11.3).
- Additional duty leviable under Section 3 of Customs Tariff Act equivalent to duty of excise specified.
- Additional duty leviable under section 3(5) of Customs Tariff Act in lieu of VAT.
- **Only manufacturer is entitled for Cenvat in this regard. Service provider is not entitled.**
- Excise duty under 1st and 2nd Schedule to Excise Tariff Act.
- Education cess on excise duty and service tax
- Secondary and Higher Education cess on excise and service tax

11.2. Non-regular and industry specific:

- Additional duty of excise leviable under 3 of the additional duty of excise (Textile and Textile Articles Act, 1978)
- Additional duty excise (Goods of Special Importance Act, 1957)
- National Calamity Contingent duty leviable under Section 136 of Finance Act, 2001.
- Additional duty of excise levied for pan masala and certain tobacco products under Section 85 of Finance Act, 2005.
- Additional duty of excise leviable under Section 157 of Finance Act, 2003 (32 of 2003).

11.3. Service tax leviable U/s. 66 of Finance Act should include the following:

- Service tax paid at full rate on various services.
- Service tax paid on abated value of services such as construction services, rent-a-cab, Mandap keeper, outdoor caterers etc.
- Service tax paid under composition scheme under works contract service category.
- Service tax paid at alternate rate on services such as air travel agent services, foreign exchange broker's services, insurance services etc.

The manufacturer / service provider can avail the Cenvat credit in respect of input services irrespective of rate at which service tax is paid by service provider on such services.

12. Cenvat availment:

12.1. CCR allows input tax credit at the time of entry of input, capital goods or services in the value addition chain i.e. at the time of purchase / payment for the same. There is no requirement as to one to one correlation of inputs with final output. In order to avail the Cenvat credit, broad nexus of inputs / capital goods / input services with manufacture and / or service provision is enough.

12.2. Manufacturer / service provider can avail Cenvat Credit of relevant duties / tax at following point of time:

Duty on Input goods	On receipt of goods in the factory of manufacturer / premises of service providers – Rule 4(1) of CCR.
Duty on Capital goods	50% in the financial year of receipt of capital goods in factory of manufacturer or premises of service providers and balance in any subsequent financial year(s) – Rule 4(2) of CCR.
Service tax on Input services	On payment of value of the input service and service tax thereon – Rule 4(7) of CCR.

12.3. Assessee (through inadvertence) may not avail Cenvat credit in time or claim it at later point of time. Department has clarified that assessee should claim Cenvat at earliest opportunity. This does not mean that benefit of Cenvat could be denied to assessee in case where such availment is delayed. Excise manual treats period of one year as a reasonable period for claiming Cenvat credit. There is plethora of judgments which held the period exceeding one year also to be reasonable period for Cenvat availment. Honorable Supreme Court in the case of Formica India Division Vs CCE (1995) 77 ELT 511 (SC) explains underlying principle in this regard. Honorable Allahabad High Court, in case of CCE Vs Ram Swarup Electrical Ltd 2007 TIOL 640 held that there is no time limit for assessee to avail MODVAT as the MODVAT (Cenvat) claim is indefeasible.

12.4. Provisions of law may be different at the time of availment and utilization. It is fairly settled legal position that law applicable at point of availment is relevant and not law applicable at point of utilization. This view is fortified by Honorable Supreme Court in case of Grasim Industries Ltd Vs CCE 179 ELT A38.

13. Documents on which Cenvat credit can be availed:

13.1. Manufacturer, service provider and / or input service distributor can avail the Cenvat credit on the basis of following documents specified in Rule 9(1) of CCR. These documents are popularly known as duty / tax paid documents.

- Invoice / bill / challan issued by :
 - Manufacturer
 - Importer
 - Consignment agent of manufacturer / importer
 - First stage or second stage dealer (Refer Para 13.4)
 - Service provider
 - Input service distributor (Refer Para 13.5).
- Bill of entry
- Certificate issued by custom appraiser for goods imported through post office.
- Challan evidencing payment of service tax paid under Rule 2(1)(d).

13.2. Invoice, bill or challan should contain all the particulars prescribed under Central Excise Rules, 2002 or Service Tax Rules, 1994 as the case may be (Rule 9 (2) of CCR). In absence of prescribed particulars, Cenvat Credit can be denied. Deputy Commissioner of Central Excise or Assistant Commissioner of Central Excise may allow Cenvat credit on the basis of deficient document provided he is satisfied that the goods or services covered by the document is received and accounted for in books of account of the assessee (Proviso to Rule 9 (2) of CCR).

13.3. It is fairly settled law that assessee should not be deprived of benefits of Cenvat Scheme for procedural lapse or defects. Cenvat credit can not be denied to assessee complying with substantive provisions / rules of CCR. In absence of malafide intention on the part of assessee, procedural infractions / lapses may be condoned. The assessee may rely on following judicial precedence in support of his contention:

- Maschmeijer Aeromatics (I) Ltd Vs CCE 46 ELT 395 (Mad CEGAT)

- Aluminum Industries Ltd Vs CCE 1993 (65) ELT 460 (Mad. CEGAT)

Honorable Supreme Court, in case of Mangalore Chemicals & Fertilizers Ltd [55 ELT 437], observed that there is a distinction between procedural condition of a technical nature and substantive condition. Non-observance of former is condonable while that of a latter is not condonable. Honorable Tribunals and Courts have followed this principle in large number of cases.

- 13.4. Cenvat credit can be availed on basis of invoice issued by dealer registered with Central Excise. First stage and second stage dealer registered with Central Excise can issue Cenvatable invoice. First stage dealer means dealer purchasing goods from manufacturer or his depot or consignment agent. Second stage dealer means dealer purchasing excisable goods from first stage dealer. This mechanism is provided to ensure that Cenvat chain does not break when purchaser buys the goods from traders and not directly from the manufacturer.
- 13.5. Rule 7 of CCR provides for “Input Service Distributor” mechanism. Many assessees have factories / service units at different locations and corporate / registered / administrative office at different location. Usually input service taxes are paid and invoices are received at office. Such office can be registered as “Input Service Distributor” and can distribute Cenvat credit of service tax availed by it by issuing an invoice to manufacturing units or units providing output service. The distribution of credit can be done in any ratio among various units. However, total credit distributed should not be more than service tax paid on input services. If some input service is exclusively used for exempted final product / output service, input service distributor can not avail and distribute such input service tax under this mechanism.
- 13.6. Rule 7A of CCR provides for “Input Credit Distributor” mechanism (ICD). Such ICD can distribute credit on duty paid on inputs (goods) if invoice received by it to factories and service units. Since Cenvat credit can be passed through mechanism of endorsement of invoice, this facility is not much used by the assessee.

14. Utilization of Cenvat credit:

14.1. Rule 3(4) of CCR allows the manufacturer or service provider to utilize the Cenvat credit for discharging liabilities in respect of:

- Excise duty on any final product.
- An amount equal to Cenvat credit taken on inputs if such inputs are removed as such or after being partially processed; or
- An amount equal to the Cenvat credit taken on capital goods if such capital goods are removed as such; or
- An amount under Rule 16(2) of Central Excise Rules, 2002; or
- Service tax on any out put service.

14.2. Cenvat credit availed in respect of Excise duty, Service tax, CVD etc become integral part of Cenvat credit pool / common kitty available for utilization. Once credit for any tax / duty is properly availed, its individual character / identity is lost except for education cess and higher education cess. Thus Cenvat credit built up out of Excise duty, CVD, Additional duty etc on input / capital goods can be utilized for payment of service tax and vice-a-versa.

14.3. Cenvat credit built up out of education cess can be utilized only for payment of education cess on excise duty and service tax. It can not be utilized for the payment of excise duty, service tax and secondary higher education cess.

- Proviso to Rule 3(7)(b) of CCR.

14.4. Cenvat credit built up out of secondary higher education cess can be utilized only for payment of secondary Education cess on excise duty and service tax. It can not be utilized for the payment of excise duty, service tax and education cess.

- Proviso to Rule 3(7)(b) of CCR.

14.5. It is not necessary to have one to one co-relation or nexus between activities on which input tax credit availed and activities on which output tax paid. In case of service provider providing taxable services falling under different categories is entitled to utilize Cenvat balance built up out of input services pertaining to one category for discharging output tax liability of other service category. For example a person rendering architect services and interior decorator services

is entitled to utilize Cenvat credit relatable to architect services to discharge tax liability on interior decorator services or vice-a-versa.

14.6. Utilization can not exceed Cenvat balance as on last day of month / quarter for which tax is paid [Proviso to Rule 3(4) of CCR].

15. Accumulated Cenvat balance:

15.1. If Cenvat availment exceeds utilization, balance is to be carried forward.

15.2. Cenvat credit balance is like tax deposit with the Government available for discharging future tax liability [Eicher Motors Ltd Vs UOI 106 ELT 3 (SC)].

15.3. Cenvat credit validly availed cannot be reversed by tax authorities. Benefit of credit is available without any limitation and the scheme is indefeasible [CCE V/s. Dai Ichi Karkaria Ltd – 1990 (112) ELT 353 (SC)].

15.4. Cenvat credit balance does not lapse. It can be carried forward eternally.

15.5. Rule 5 of CCR read with Notification No. 5/2006-CE (NT) dated 14.03.2006 permits manufacturer exporter of the goods and / or services exporter to claim refund of accumulated Cenvat balance in case where such assessee is not in a position to utilize the Cenvat balance for payment of excise duty on domestic clearance of goods or for payment of service tax on provision of local services. The grant of refund is subject to compliance of conditions and procedures prescribed in above referred notification and Rule.

15.6. Cenvat scheme is ongoing adjustment scheme. Cenvat Credit Rules do not contain any specific provisions allowing refund of accumulated Cenvat balance in cash. Generally assessee is not entitled to refund of balance in cash except in case of exporters as stated in preceding Para. However judiciary in some cases has taken a radical view that in absence of specific provisions denying refund of accumulated Cenvat balance in cash, such refund is permissible in special circumstances. Following judicial pronouncements are worth noting in this regard:

- Union of India Vs Slovak India Trading Co. Pvt. Ltd. (2008) 10 STR 101 (Karnataka High Court), Honorable Supreme Court

affirmed the decision of Karnataka High Court [2008 (223) ELT A170 (SC)].

- CCE Vs Nag Polypouches (P.) Ltd (2007) 8 STR 223 (Tri. Del)

15.7. Transfer of unutilized Cenvat balance is permitted in case of change in ownership or change in site resulting from sale, merger, amalgamation, lease or joint venture [Rule 10(1) of CCR].

The transfer of Cenvat balance by service provider is permissible on transfer of liabilities of business to new entity [Rule 10(2) of CCR].

The inputs stock, in process stock and capital goods should also be transferred along with the factory or business premises to new site or new owners [Rule 10(3) of CCR].

16. Cenvat Scheme Operation – In Nut-Shell

Date	Particulars	Availed	Utilized	Balance	Remarks
01.09.2010	Op. Balance			1,500	Cenvat balance does not lapse.
02.09.2010	Excise duty on raw material	3750		5,250	Availed on receipt of goods in factory.
05.09.2010	CVD on import of raw material	2,000		7,250	As above.
05.09.2010	Additional duty on raw material	1,000		8,250	As above.
19.09.2010	Excise duty on capital goods	5,000		13,250	50% of duty of Rs. 10,000. On receipt in factory.
25.09.2010	Service tax on input services	1,350		14,600	On payment of value of service and service tax to vendors.
04.10.2010	Excise on raw material	2,000		16,600	On receipt of goods in factory.
05.10.2010	Excise payment for Sept-2010		10,000	6,600	Total utilization can not exceed balance on the last day of month / quarter for which tax payment is made.
05.10.2010	ST payment – liability 8,000 for Sept-2010		4,600	2,000	Service tax of Rs.3,400 to be paid in cash in spite of Cenvat balance of Rs.2,000 on date of payment.

17. Inputs

17.1. Manufacture / service provider is entitled to Cenvat credit of following duties / taxes paid on inputs:

- Excise duty.
- Countervailing custom duty on imports in lieu of Excise duty.
- Additional duty of customs in lieu of VAT (only for manufacturer).
- Education cess on excise duty.
- Secondary and higher education cess on excise duty.

It is, therefore, important to understand the meaning of the term “input”.

17.2. Term “input” is defined under Rule 2(k) of CCR. The term “input” is defined in different manner for manufacturer and service provider.

17.3. “Input” for manufacturer:

- It means goods used directly or indirectly in or in relation to manufacture of final product and whether or not such goods contained in final product.
- It also includes following goods used in or in relation to manufacture of final product:

Lubricating oils	Greases	Cutting oils	Coolants
Accessories cleared along with the final products	Paint	Packing material	Fuel
Goods used for generation of electricity	Goods used for generation of Steam		

- It also includes goods used in manufacture of capital goods to be used in factory of manufacturer.
- Term “Goods” is to be understood as defined under Sale of Goods Act, 1930 [Rule 2(t) of CCR read with section 2(50) of Finance Act, 1994].
- Following goods are specifically excluded from definition of “input” and hence manufacturer is not entitled to Cenvat credit in respect of same:
 - Light diesel oil, high speed diesel oil and petrol.

- Cement, angles, channels, CTD bar, TMT bar and other items used for construction of factory shed, building or laying foundation or making of structure for support of capital goods.
- Manufacturer is not entitled to take Cenvat in respect of inputs used for manufacture of exempt products.
- The use of phrases “directly or indirectly”, “used in relation to” and “whether or not contained in final products” in definition widens the scope of term “Input”. Judiciary generally takes the view that scope of term “input” is very wide for manufacturer. Few important judicial pronouncements explaining the scope and meaning of term “input” are as under:
 - CCE Vs East End Paper Industries 1989 (43) ELT 201 (SC)
 - Ponds India Limited Vs CCE 1993 (63) ELT 3 (Mad)
 - Tata Engineering and Locomotive Co. Ltd Vs State of Bihar (1994) 74 ELT 193 (SC).
 - Tata Engineering & Locomotive Co. Ltd Vs UOI (1994) 72 ELT 525 (PAT)
 - Maruti Suzuki Ltd Vs CCE (2009) 240 ELT 641 (SC).
- Any input integrally connected with manufacturing is eligible for Cenvat. Manufacturer is also entitled to Cenvat in respect of material lost in process.
- The inclusive limb of definition makes it absolutely clear that the consumables, accessories, paints and other such items are eligible for Cenvat credit.
- Inputs should be received and used in the factory in which final products are manufactured from such inputs. It will be difficult to claim Cenvat in respect of inputs directly sent to third party’s place [Rule 2(k) of CCR].
- For the purpose of CCR, the motor vehicle is not capital goods. Unlike service provider, the definition of “input” does not specifically exclude “motor vehicle” for manufacturer. A view can, therefore, be taken that “motor vehicle” is an input for the manufacturer. If manufacturer uses vehicle within factory premises, he may be eligible for Cenvat in this regard.

17.4. “Input” for service provider:

- It would mean all goods used for providing any output service.
- Term “Goods” is to be understood as defined under Sale of Goods Act, 1930 [Rule 2(t) of CCR read with section 2(50) of Finance Act, 1994].
- Following goods are specifically excluded from definition of “input” and hence service provider is not entitled to Cenvat credit in respect of same:
 - Light diesel oil, high speed diesel oil and petrol.
 - Motor vehicle.
- Unlike manufacturers, there is no condition as to receipt of inputs in the premises of the service provider. Input received by service provider at place different from its registered premises is also eligible for Cenvat.
- The phrases like “directly or indirectly” and “used in relation to” are not used in the definition of “input” for service provider. Definition of “input” is restrictive for service provider. Only those goods which are directly used for providing output service is eligible for Cenvat credit. This view gets support from decision in case of Mundra Port & SEZ Ltd. Vs CCE (2009) 18 STT 314 (Ahd-CESTAT), wherein it was held that cement and steel used for construction of jetty is not “input” for providing taxable port service.
- CBEC, vide its letter No. F. No. 137/120/2008-CX.4 dated 23.10.2008, clarified that service provider providing “supply of tangible goods for use” is entitled to treat machinery, equipment, appliances, vehicles, aircrafts, vessels etc supplied on hire as “input” and can claim Cenvat in respect of it.

17.5. Manufacturer / service provider can avail Cenvat on receipt of goods in factory / premises [Rule 4 of CCR].

- Date of payment to supplier is not relevant.
- Date of accounting entry is not relevant.
- Date of consumption of material is not relevant.

- 17.6. If inputs on which Cenvat credit has been taken are removed as such from the factory / premises, the manufacturer / service provider shall pay an amount equal to Cenvat credit availed in respect of such inputs [Rule 3(5) of CCR].
- 17.7. If the value of inputs, before being put to use, is written off fully or provision is made in the books of account to write off fully, the assessee is required to pay an amount equal to Cenvat credit taken in respect of such inputs. However if said inputs are subsequently used, assessee can reclaim the Cenvat credit [Rule 3(5B) of CCR].

18. Capital Goods

- 18.1. Manufacture / service provider is entitled to Cenvat credit of following duties / taxes paid on capital goods:
- Excise duty.
 - Countervailing custom duty on imports in lieu of Excise duty.
 - Additional duty of customs in lieu of VAT (only for manufacturer).
 - Education cess on excise duty.
 - Secondary and higher education cess on excise duty.
- 18.2. It is, therefore, important to understand the meaning of the term “capital goods”. The meaning of said term for Cenvat scheme is totally different from normal meaning as understood by common man or by an accountant. It is not necessary that all assets classified as capital assets in financial statement of assessee are “capital goods” for the purpose of CCR. The term “capital goods” is specifically defined in CCR. Goods specifically covered in said definition can only be treated as “capital goods” for the purpose of CCR.
- 18.3. Under Rule 2(a) of CCR, “Capital goods” means:
- All goods falling under Chapter 82, Chapter 84, Chapter 85, Chapter 90, 2[*heading 6805, grinding wheels and the like, and parts thereof falling under heading 6804*] of the First Schedule to the Excise Tariff Act;
 - Pollution control equipment;
 - Components, spares and accessories of the goods specified in (i) and (ii) of Rule 2(a);

- Moulds and dies, jigs and fixtures;
- Refractories and refractory materials;
- Tubes and pipes and fittings thereof; and
- Storage tank.

This is a comprehensive definition. Only above referred goods can, therefore, be treated as “capital goods”. Honorable Supreme Court in case of Vikram Cement Vs CCE (2 STT 185) held that the definition of capital goods is not an inclusive definition and hence any exercise to treat any item as “capital goods” by interpretive process would be futile.

18.4. Components, spares and accessories of capital goods can be treated as “capital goods” for the purpose of CCR even though same is not falling in the above referred excise tariff. This position is confirmed by Circular No.276/110/96-TRU dated 02.12.1996. Following judicial pronouncements support this contention:

- Bhushan Steel Strips Vs CCE (2005) 1 STT 298 (CESTAT)
- CCE Vs Hindustan Motors (2007) 217 ELT 378 (CESTAT-Kolkatta)

18.5. Dumpers and tippers falling under Chapter 87 are eligible capital goods for service providers providing Site Formation Services and / or Mining Services. Such service providers are eligible for Cenvat credit in respect of dumper / tipper provided it is registered in their name. Other service providers or manufacturers are not eligible for such Cenvat credit [Rule 2(a)(C) of CCR].

18.6. Motor vehicle is capital goods for following specified service providers:

Courier agencies	Tour Operator	Rent-a-Cab Operator	Cargo Handling Agency
Goods Transport Agency	Outdoor Caterer	Pandal / Shamiana Contractor	

Only above referred service providers are entitled to claim Cenvat credit in respect of motor vehicle. Service providers (other than above) are not eligible for Cenvat credit in respect of motor vehicles.

Conditions stipulated for availment of Cenvat credit in respect of vehicle:

- Vehicle is registered in the name of service provider.
- Vehicle is used for providing out put services.

Specified service providers (except GTA) usually claims abatement benefit and pay output tax on abated value of the services. If they claim Cenvat, abatement benefit would be jeopardized. Such service providers have to make conscious decision whether to go for abatement or Cenvat. Goods Transport Services are excluded from the definition of taxable output services and hence the good transport agency will not be entitled to Cenvat credit in respect of motor vehicles though it is eligible capital goods.

- 18.7. Equipment or appliance used in office of the manufacturer is specifically excluded from the definition of capital goods. An air conditioner or computer installed in office of the manufacturer is not eligible for Cenvat credit. However, definition of capital goods does not exclude the appliances or equipments installed or used in the service provider's office premises. The service provider is eligible for Cenvat in respect of office appliances and equipments.
- 18.8. It is incumbent for the manufacturer to use the capital goods in the factory of production. The manufacturer is not entitled to Cenvat in respect of Capital goods installed / used outside factory. However for service provider there is no stipulation as to place of usage of capital goods. Service provider can use the capital goods outside his premises without jeopardizing his right to claim Cenvat in respect of such capital goods.
- 18.9. Manufacturer can send capital goods outside for job work or other purpose. However same should be brought back within 180 days. If capital goods are not brought back to factory within stipulated period, manufacturer is obliged to pay an amount equivalent to Cenvat credit attributable to the capital goods by debiting Cenvat account. The manufacturer can take the credit again when such capital goods are received back in the factory [Rule 4(5)(a) of CCR]. However, moulds, dies, jigs and fixtures can be sent outside without restriction of return within 180 days [Rule 4(5)(b) of CCR].
- 18.10. Cenvat credit can not be claimed in respect of capital goods which are :
 - Used exclusively in the manufacture of exempted goods.

- Used exclusively in providing exempted services.

– Rule 6(4) of CCR.

18.11. Manufacturer / service provider is entitled to avail full Cenvat credit in respect of capital goods:

- Used in manufacture of excisable and exempt goods.
- Used for providing taxable and exempt services.

The above referred proposition was upheld by judiciary in following cases:

- Hutchison Essar Gujarat Ltd. Vs CCE (2007) 8 STR 555 (CESTAT - Delhi)
- CCE Vs R.N. Agarwal Industries Ltd. (2007) 212 ELT 110 (CESTAT- Ahmedabad).

18.12. Law applicable at point of availment is relevant and not law applicable at point of utilization [Grasim Industries Ltd Vs CCE 179 ELT A38 (SC)].

Fall out of above principle would be as under:

- Capital goods bought when services were exempted, Cenvat credit can not availed on service becoming taxable.
- Cenvat credit availed on capital goods bought when services were taxable can not be reversed or withdrawn on service getting exempted at later date.

18.13. Old, used or second hand capital goods are eligible for Cenvat provided same is cleared on payment of duty.

18.14. Cenvat credit can be availed on capital goods acquired on lease, hire purchase or under loan agreement from finance company. Ownership is not mandatory for availing Cenvat credit [Rule 4(3) CCR]. This proposition was upheld by judiciary in following cases:

- German Remedies Ltd Vs CCE 2002 (144) ELT 606 (Mum-CEGAT).
- Maruti Udyog Vs CCE 2004 (165) ELT 226 (CESTAT-Delhi).

- Dalmia Cements Bharat Ltd. Vs CCE (2008) 224 ELT 484 (CESTAT- Chennai).

18.15. Cenvat credit is not allowed on that part of value representing duty on such goods claimed as depreciation U/s.32 of Income Tax Act, 1961 [Rule 4(4) of Cenvat Rules]. This point can be clarified with the help of table showing Cenvat availability on Capital Goods where depreciation is claimed under Income Tax Act and where such depreciation is not claimed:

	Depreciation @ 15%	Depreciation @ 5%
A) <u>Duty included in cost of asset for claiming depreciation</u>		
Cost of Assets	10,00,000	10,00,000
Add : Excise duty (A)	1,03,000	1,03,000
	11,03,000	11,03,000
Depreciation claimed under Income Tax (B)	1,65,450	55,150
Cenvat eligibility (A – B)	NIL	47,850
B) <u>Duty not included in cost of Assets for claiming depreciation</u>		
(i) Depreciation claimed on basic value Rs.10,00,000/-		
(ii) Cenvat eligibility		1,03,000 (Actual Excise Duty)

18.16. Manufacturer / service provider is entitled to avail Cenvat on receipt of capital goods in factory / premises.

- Date of payment to vendor is not relevant.
- Date of accounting entry is not relevant.

18.17. Manufacturer / service provider can avail Cenvat in respect of capital as under:

- 50% in financial year in which capital goods are received.
- Balance 50% in any subsequent financial year, provided capital asset is still in the possession of assessee.

In case of a factory yet to commence the production, Cenvat in respect of machinery received before commencement of production can be availed in the year in which factory is registered and production is started [Circular No.88/88/94 dated 16.12.1994]. This

principle should also apply to service provider. However it is advisable to intimate the department in this regard.

18.18. If capital goods on which Cenvat credit has been taken are removed as such from the factory / premises, the manufacturer / service provider is obliged to pay an amount equal to Cenvat credit availed in respect of such capital goods [Rule 3(5) of CCR].

18.19. If capital goods (other than computer and computer peripherals) on which Cenvat credit is claimed are removed after use, the manufacturer / service provider is liable to pay an amount equal to Cenvat credit taken as reduced by 2.5% for each quarter of a year from the date of taking Cenvat credit [Proviso to Rule 3(5) of CCR].

18.20. If computer and computer peripherals on which Cenvat credit is claimed are removed after use, the manufacturer / service provider is liable to pay an amount equal to Cenvat credit taken as reduced by following percentage for each quarter of a year from the date of taking Cenvat credit:

- For each quarter in first year @ 10%.
- For each quarter in second year @ 8%.
- For each quarter in third year @ 5%.
- For each quarter in fourth and fifth year @ 1%.

[Proviso to Rule 3(5) of CCR]

18.21. If capital goods on which Cenvat was availed are removed as scrap, an `amount' equal to duty on scrap value is payable [Rule 3(5A) of CCR].

18.22. If the value of capital goods, before being put to use, is written off fully or provision is made in the books of account to write off fully, the assessee is required to pay an amount equal to Cenvat credit taken in respect of such capital goods. However if such capital goods are subsequently used, assessee can reclaim the Cenvat credit [Rule 3(5B) of CCR].

19. Inputs Services

19.1. Manufacture / service provider is entitled to Cenvat credit of following taxes or cess paid on input services:

- Service tax leviable U/s. 66

- Education cess on service tax.
- Secondary and higher education cess.

19.2. Term "input service" is defined under Rule 2(l) of CCR

- It would mean any service used by service provider for providing an output service.
- It would mean any service used by manufacturer, whether directly or indirectly, in or in relation to manufacture of final product and clearance of final products up to the place of removal.
- It would also include following services used by manufacturer / service provider in relation to:
 - Setting up of factory / premises of service provider or an office relating to such factory / premises
 - Modernization of factory / premises of service provider or an office relating to such factory / premises
 - Renovation or repairs of a factory / premises of service provider or an office relating to such factory / premises
 - Advertisement or sales promotion
 - Market research
 - Storage up to the place of removal
 - Procurement of inputs
 - Activities relating to business, such as:
 - » Accounting
 - » Auditing
 - » Financing
 - » Recruitment and quality control
 - » Coaching and training
 - » Computer networking
 - » Credit rating
 - » Share registry
 - » Security
 - » Inward transportation of inputs or capital goods
 - » Outward transportation up to the place of removal

19.3. Definition of “input service” is very wide. Inclusive limb of the definition expands the scope much beyond manufacture or provision of taxable service. The use of phrases “directly or indirectly”, “used in relation to” and “activities relating to business” in definition widens the scope of term “Input services”. One to one co-relation between input services and final product / output services is not specifically sought by this definition. Judiciary is generally interpreting the term “input services” in liberal manner and takes broader meaning of the term. Few important judicial pronouncements explaining the scope and meaning of term “input services” are as under:

- Coca Cola India Pvt. Ltd. Vs. CCE, Pune-III [2009-TIOL-449-HC-Mum-ST]
- CCE, Nagpur Vs Ultratech Cement Ltd [2010-TIOL-745-HC-MUM-ST]
- ABB Ltd. Vs CCE (2009) 21 STT 77 (Bangalore CESTAT – LB)

Above referred judgments lay down following important principles on interpretation of term “input service”.

- The expression “such as” means “for example” or “of a kind that”. These expressions widen the scope of definition.
- Input tax credit can be claimed for all services having direct or indirect nexus with business of manufacturer / service provider.
- Broader concept of relatability of input services to the business and not to manufacture. Any activity in relation to business is an input service.
- If cost incurred on any service is included in the final value of the product or output services on which tax or duties are paid, Cenvat credit of same can be claimed.
- Cenvat on post production activities can also claimed.
- Definition of “input service” is not confined to “manufacture” but has to be interpreted on the basis of requirements of business.

19.4. The approach of Department is to take restrictive meaning of the term “input services”. However, Judiciary is generally taking broader meaning of “input services” and allows Cenvat credit on input

services liberally. There is plethora of such decisions. Some of them are reproduced hereunder:

Input Service	Allowability Upheld
Mobile phone	Indian Rayon Industries [2006-TIOL-1152-CESTAT-MUM] Circular No.97/8/2007 dt. 23.08.07.
Landline phones in factory	CCE Vs Beekay Engg. & Casting Ltd. 2009-TIOL-1376-CESTAT-Del
Residential telephone of Director / Employees / Partners	ITC Ltd. Vs CCE, Salem 2009-TIOL -439-CESTAT-MAD.
CHA service for export of goods	CCE Vs Adani Pharma Chem Pvt. Ltd. 2008-12-STR-593 (Ahm. Tri.)
Health insurance of Staff / Director	GTC Industries 2008-TIOL-1634-CESTAT-MUM (LB)
Aircraft Parking at Airport	Force Motors Ltd Vs CCE (2009) 13 STR 692 (Mum-Tri.)
Insurance of Plant & Machinery	Finolex Cables Ltd Vs CCE 2009-14-STR-303 (Mum-Tri.)
Security services	C.J. Galetine Products Vs CCE 7 STR 558 (Del-Tri.)
Construction of residential colonies	Victor Gaskets Ltd. 2008-10-STR-369 (Mum.-Tri.)
Staff colonies maintenance	ITC Ltd. Vs CCE (2009) 22 STT 282 (CESTAT – Bangalore)
Canteen Services	CCE Vs GTC Industries Ltd. 2008 (12) -STR-468 (Mum. Tri. LB) / CCE, Nagpur Vs Ultratech Cement Ltd [2010-TIOL-745-HC-MUM-ST]
Staff Medical Insurance	Millipore India Ltd. Vs CCE (2009) 13 STR 616 (Bangalore - Tri.)
Staff Bus Transportation	CCE Vs Cable Corpn. Of India Ltd. 2008 (12) STR 468 (Bom.-Tri.-LB)
Group Insurance Health Policy	Stanzen Toyotetsu India (P) Ltd Vs CCE (2009) 21 STT 321 (CESTAT – Bangalore)

Man Power Supply	Sanghi Industries Ltd Vs CCE 2009 (13) STR 167 (Ahm. Tri.)
Commission on Sales	Metro Shoes Pvt. Ltd. VS CCE 2007 (8) STR 502 (Bom.Tri.)
Advertisement	Kamdhenu Ispat Ltd. Vs CCE 2007 (8) STR 188 (Del. Tri.)
Rent-a-cab Services	C.J. Geletine Products Vs CCE 2007 (7) STR 558 (Del. Tri.)
Loan processing fees	Alluminium Powder Co. Ltd. Vs CCE 2007 (8) STR 353 (Mad. Tri.)
Merger / Takeover expenses	Aditya Birla Nuvo Ltd Vs CCE 2009 (14) STR 304 (Ahm. Tri.)
General Insurance towards fire, machinery breakdown, cash handling, group gratuity, group accident etc.	CCE, Raipur Vs Beekay Engg. & Castings Ltd. 2009-TIOL-1376-CESTAT-Del.)
Hire charges	CCE Vs Deloitte Tax Service (2008) 16 STT 449 (CESTAT-Bangalore)
Courier	CCE Vs CCL Products (I) Ltd. (2009) 22 STT 36 (CESTAT-Bangalore)
Training charges	CCE Vs Deloitte Tax Service (2008) 16 STT 449 (CESTAT-Bangalore)
Garden Maintenance	H.E.G. Ltd Vs CCE (2009) 23 STT 157 (CESTAT-Delhi)
Internet Services	Universal Cable Ltd. Vs CCE (2007) 7 STR 310 (CESTAT)

Above referred decisions are delivered with reference to specific facts of the case. It is, therefore, advisable for readers to apply the ratio of above decisions after considering the facts of their case.

19.5. Port is a “place of removal” for exporters. A view, therefore, is taken that services availed after removal of goods from factory but before shipment of goods from Port are input services eligible for Cenvat credit. This view is affirmed in following cases:

- CCE Vs Rolex Rings (P.) Ltd. (2008) 16 STT 193 (CESTAT - Ahmedabad).

- CCE Vs Adani Pharmachem (P.) Ltd. (2009) 19 STT 239 (CESTAT - Ahmedabad).
- Rawmin Mining Vs CCE (2009) 18 STT 329 (CESTAT-Ahmedabad).

19.6 The place of receipt or usage of input services is not relevant for claiming Cenvat credit. Assessee receiving and using input services any where is entitled to claim Cenvat in respect of such input service.

19.7 Cenvat credit on input service can be availed on or after payment of value of input services and service tax thereon.

- Date of receipt of service not relevant.
- Date of vendor's invoice not relevant.
- Date of accounting entry not relevant.

20. Cenvat Credit – Taxable and Exempt activities

20.1. Most of the assessees have multiple business activities. Some activities may be taxable and others are exempt / non taxable. Eligibility of Cenvat in such cases is a complicated issue. The Cenvat implications in such cases are summarized as under:

Reference	Gist
Rule 6(1) of CCR	No Cenvat credit is allowable on <u>input</u> and <u>input services</u> used exclusively for : <ul style="list-style-type: none"> • Manufacture of exempt / non taxable goods. • Provision of exempt services.
Rule 6(2) of CCR	Assessee may maintain separate accounts for receipts, consumption and inventory of inputs / input services used for taxable and exempt stream. <ul style="list-style-type: none"> - He can claim Cenvat pertaining to taxable stream only.
Rule 6(3) of CCR	Assessee uses common inputs and / or services for taxable and exempt stream and separate accounts are <u>not</u> maintained for receipt, consumption and inventory of inputs / input services. <p>Options:</p> <ul style="list-style-type: none"> - Avail full Cenvat credit and pay amount at specified rate on value of exempt stream; <p style="text-align: center;">Or</p>

	- Avail full Cenvat Credit and reverse the Cenvat attributable to exempt stream as prescribed in Rule 6(3A).
Rule 6(4) of CCR	No Cenvat credit is allowable on <u>capital goods</u> which are: <ul style="list-style-type: none"> • Exclusively used in manufacture of exempted goods. • Exclusively used in provision of exempted services. By implication, full Cenvat credit is allowable in respect of capital goods : <ul style="list-style-type: none"> • Used in manufacture of dutiable and exempted goods. • Used for providing taxable and exempted services.
Rule 6(5) of CCR	Credit of whole service tax paid on specified services (Refer Para 20.2) is allowed fully whether such input services are used: <ul style="list-style-type: none"> • Partly for manufacture of dutiable goods and partly for manufacture of exempted goods. • Partly for provision of taxable services and partly for exempted services.

20.2. Specified Services U/R 6(5) of CCR

Cenvat credit is fully available in respect of following services even through same are partly used taxable stream and party for exempt stream:

Consulting Engineer	Architect	Interior Decorator
Management Consultant	Real Estate Agent	Security Agency
Scientific or Technical Consultant	Banking and financial services	Intellectual Property Rights Services
Life Insurance Auxiliary Services	Erection, Commissioning and Installation Services	Technical Inspection or Certification Services
Technical Testing and Analysis Services	Foreign Exchange Broker Services	Commercial or Industrial Construction Services

20.3. Rule 6(3) of CCR–Cenvat For Common inputs / Services

- Rule 6(3) is revamped w.e.f. 01.04.2008. It is applicable to Manufacturer of dutiable and exempt goods as well as service provider providing taxable and exempt services. This is applicable where assessee does not maintain separate accounts in respect of input goods and services used for taxable and exempt streams. The said rule gives following options to the assessee:

Assessee	Option I	Option II
Manufacturer of dutiable and exempt products	To avail full Cenvat credit and to pay amount of 5% on value of exempted goods	To avail full Cenvat credit and pay / reverse an amount equal to Cenvat credit attributable to inputs / input services used for manufacture of exempt goods as per formula given in Rule 6(3A).
Service provider providing taxable and exempt services	To avail full Cenvat credit and to pay amount of 6% on value of exempted services	To avail full Cenvat credit and pay / reverse an amount equal to Cenvat credit attributable to inputs / input services used for providing exempted services as per formula given in Rule 6(3A).

- 20.4. Option is qua-assessee and not qua category of services / products. Option selected is binding on assessee for all categories of services and products [Explanation I to Rule 6(3) and Circular No.868/6/2008 dt.09.05.08].
- 20.5. Option, once exercised, can not be withdrawn / changed during the financial year [Explanation to Rule 6(3)].
- 20.6. Assessee should select the option very carefully as it can have serious tax implications. Comparative tables showing tax implications under option I and II in two different scenario are as under:

Options Comparison – where Cenvat entitlement is higher

Particulars	Output services	Service tax payable	Input services availed	Inputs service tax
Taxable services	60,000	6,180	90,000	9,270
Exempt services	40,000	Nil		
Total	1,00,000	6,180	90,000	9,270
Option I – Payment of 6% on exempt services				
Tax @ 10.30 on Taxable services of Rs.60,000				6,180
Tax @ 6.18% on Exempt services of Rs.40,000				2,472
Total Tax payable				8,652
Less: Cenvat credit – Input service tax				9,270
Net service tax payable / (Refund) under Option I				(618)
Option II – Cenvat Reversal				
Tax @ 10.30 on Taxable services of Rs.60,000				6,180
Total Cenvat credit			9,270	
Less : Proportionate reversal (40,000 / 100,000) X 9,270				3,708
Net service tax payable under Option II				618
Additional liability under Option II				1,236

Options Comparison – where Cenvat entitlement is lower

Particulars	Output services	Service tax payable	Input services availed	Inputs service tax
Taxable services	60,000	6,180	5,000	515
Exempt services	40,000	Nil		
Total	1,00,000	6,180	5,000	515
Option I – Payment of 6% on exempt services				
Tax @ 10.30 on Taxable services of Rs.60,000				6,180
Tax @ 6.18% on Exempt services of Rs.40,000				2,472
Total Tax payable				9,270
Less: Cenvat credit – Input service tax				515
Net service tax payable under Option I				8,755
Option II – Cenvat Reversal				
Tax @ 10.30 on Taxable services of Rs.60,000				6,180
Total Cenvat credit available			515	
Less : Proportionate reversal (40,000 / 100,000) X 515				206
Net service tax payable under Option II				5,871
Additional liability under Option I				2,884

20.7. The payment of above referred 5% or 6% is in addition to excise duty and / or service tax payable on taxable stream.

20.8. Assessee choosing to pay 5% or 6% under Option I may pay the same by debiting Cenvat credit account or in cash [Explanation II to Rule 6(3A)]

20.9. Proportionate Cenvat reversal option – Rule 6(3A) of CCR:

- Rule 6(3A)(a) option is popularly known as “Proportionate Cenvat Reversal Scheme”. Assessee opting for this option should intimate his intention to exercise this option to the jurisdictional Superintendent giving following details:
 - Name, address and registration number
 - Date from which the option is exercised or proposed to be exercised
 - Description of dutiable goods or taxable services
 - Description of exempted goods or services
 - Cenvat credit balance of inputs and inputs services as on date of exercising option.

Following ambiguities and non-clarity may lead to some issues under reversal option:

- Due date for exercising the option is not specified.
- Consequences of non-intimation or delayed intimation
- Rule 6(3A)(a) contemplates provisional reversal of Cenvat credit availed in respect of exempt goods and services on monthly basis and final reversal on annual basis. The provisional reversal is to be done on the basis of preceding financial year’s figures. The final reversal is to be done on the basis of figures for the financial year under consideration.
- Individual, proprietary concerns and partnership firms are also required to follow reversal procedure on monthly basis irrespective of their payment due on quarterly basis.

- No reversal is required in respect of Cenvat on input services specified under Rule 6(5) of CCR. [Circular No. 868/6/2008-CX dated 09.05.2008]. List of services specified U/R 6(5) of CCR is given in Para 20.2.
- Rule 6(3A) applies only to inputs and input services, It does not apply to capital goods. Reversal of Cenvat on capital goods is not required.
- No reversal is required in respect of accumulated Cenvat credit balance as on 01.04.2008 [Circular No.137/72/2008-CX 4 dated 21.11.2008].
- If assessee did not manufacture dutiable goods or did not render taxable services in preceding financial year, he is not required to do provisional reversal on monthly basis [Rule 6(3A)(h)].

21. Cenvat Reversal Option – How it works?

21.1 Step I – Take Cenvat credit of :

- Duties on common inputs used for all activities U/R 6(3).
- Service tax paid on common services used for all activities U/R 6(3).
- Duties on inputs exclusively used for taxable activity U/R 6(2).
- Service tax paid on services exclusively used for taxable activity U/R 6(2).
- Input services covered U/R 6(5).
- Duties on capital goods U/R 6(4).

21.2 Step II – Provisional reversal on monthly basis of:

- Duties on inputs relating to exempted goods.
- Service tax on input services attributable to exempt goods.
- Service tax on input services attributable to exempt services.
- Provisional reversal is to be worked out on the basis of annual figures of preceding financial year.

21.3 Step III – Carry out above referred exercise of provisional reversal on monthly basis for entire year.

21.4 Step IV – After year end, Determine final amount of Cenvat credit attributable to exempted goods and services for entire year by taking actual figures for the said financial year.

21.5 Step V – If provisional reversal amount is less than final reversal amount, pay the difference on or before 30th June by :

- Cash
 - Debit to Cenvat Account
 - Pay interest @ 24% per annum for payment made after 30th June
- If provisional reversal amount is more than final reversal amount, take the credit in Cenvat Account

21.6 Step VI – Intimate the jurisdictional superintendent within 15 days giving following particulars:

- Amount of Cenvat provisionally reversed through out year
- Amount of final reversal
- Amount short paid along with date of payment
- Interest payable and paid on short payment
- Credit taken for excess provisional reversal

22 Practical illustration:

Facts Matrix (Question):

<u>Particulars</u>	<u>Amount</u>	<u>Tax / Duty</u>
Revenue stream		
Manufacture of dutiable goods (DG)	20,00,000	1,64,800
Manufacture of exempted goods (EG)	10,00,000	Nil
Taxable services (Billed) (TSB)	14,00,000	1,44,200
Exempt services (Billed) (ES)	4,00,000	Nil
Taxable services (Realized) (TSR)	12,00,000	1,23,600
Trading (TR)	2,00,000	Nil
Interest on loan (L)	50,000	Nil
Cenvat opening balance		20,000
Excise duty / Service tax on		
Inputs – Exempted goods (IEA)		56,000
Input – For dutiable goods and taxable service (IDG)		1,00,000
Input services – Exclusively for taxable services (IST)		50,000
Inputs–Common (IC)–Incl of Rs.1,10,000/- for exempt product		3,50,000
Inputs services – Specified Service 6(5) (ISS)		25,000
Input services – Common services (ISC)		1,00,000
Capital goods – Eligible (CG)		50,000

Suggested Answer:

Readers are requested to read this table with reference to Para 21, facts matrix given above and working notes given in succeeding para.

Particulars	Availed	Utilized	Balance	Notes
Op. Balance			20,000	
Duty on exempt goods (IEA)	Nil		20,000	1
Duty on inputs – taxable activities	1,00,000		1,20,000	
Input services – taxable activities	50,000		1,70,000	
Duty on common inputs	3,50,000		5,20,000	2
Input services U/R 6(5)	25,000		5,45,000	
Input services – Common services	1,00,000		6,45,000	
Duty on Capital goods	50,000		6,95,000	
Cenvat Reversal				
Input for exempt goods		1,10,000	5,85,000	2
Inputs for exempt services		24,935	5,60,065	3
Inputs services - Exempt MFG / Service		28,866	5,31,199	4
Payments				
Excise duty		1,64,800	3,66,399	
Service tax		1,23,600	2,42,799	

Working Notes:

1. Inputs exclusively used for exempted goods can not be availed U/R 6(1) and hence credit of excise duty of Rs.56,000/- on inputs used specifically for exempted goods is not claimed.
2. Inputs attributable to exempt goods:
 - a) No formula is prescribed in the rule.
 - b) How to identify following common inputs used for exempt and taxable products?

Common material	raw	Lubricating oil	Greases	Cutting oil
Coolant		Paint	Fuel	Packing material

c) Circular 868/6/2008-CX dt. 09.05.08 suggests that it should be:

- Done on the basis of actual consumption; or
- Quantified on the basis of store / production records; or
- Certified by Chartered Accountant / Cost Accountant.

3. Input attributable to exempted service :

Formula prescribed in Rule 6(3A):

i)
$$\text{Formula} = \frac{B}{C} \times D$$

ii) B = Total value of exempt services provided.

iii) C = Total value of dutiable goods + value of taxable services + value of exempt services provided.

iv) D = Cenvat credit taken on inputs in the month – Inputs on exempted goods (as worked out in preceding working note).

v) Value of services provided is to taken for calculation. Amount billed in earlier year is to be taken and not the realized amounts.

vi) Value means gross value as defined U/s 67. This could differ from revenue figures reflected in profit & loss account on account of following:

- Reimbursement of certain expenses is part of value for section 67
- P&L figure could be net of discounts, rebates etc
- P& L revenue figure might be inclusive of service tax, excise, VAT and such other elements.

Working:

$$\begin{aligned} &= \frac{ES}{DG + TSB + ES + L} \times (IC - 1,10,000) \\ &= \frac{4,00,000}{20,00,000 + 14,00,000 + 4,00,000 + 50,000} \times (3,50,000 - 1,10,000) \end{aligned}$$

$$= \frac{4,00,000}{38,50,000} \times 2,40,000$$

$$= 24,935$$

- Lending is taxable service and hence interest of Rs.50,000/- (L) is included in the denominator.
- Duty relatable to taxable activities (IDG) is not considered in the calculation Cenvat credit reversed as same falls under Rule 6(2) and not under Rule 6(3).
- Trading is not treated as exempt goods or exempt services.

4. Input services attributable to exempted manufacturing / services :

Formula prescribed in Rule 6(3A):

1) Formula = $\frac{E}{F} \times G$

- 2) E = Total value of exempted services provided + total value of exempted goods.
- 3) F = Total value of taxable services + Total value of exempt services + Total value of exempted goods + Total value of dutiable goods.
- 4) G = Total Cenvat credit taken on inputs services during the month
- 5) Value of services provided is to taken for calculation. Amount billed in earlier year is to be taken and not the realized amounts.
- 6) Value means gross value as defined U/s 67. This could differ from revenue figures reflected in profit & loss account on account of following:
 - Reimbursement of certain expenses is part of value for section 67
 - P&L figure could be net of discounts, rebates etc
 - P& L revenue figure might be inclusive of service tax, excise, VAT and such other elements.

Working:

$$\begin{aligned} &= \frac{ES + EG}{TSB + ES + EG + DG + L} \times ISC \\ &= \frac{4,00,000 + 10,00,000}{14,00,000 + 4,00,000 + 10,00,000 + 20,00,000 + 50,000} \times 1,00,000 \\ &= \frac{14,00,000}{48,50,000} \times 1,00,000 \\ &= 28,866 \end{aligned}$$

- Lending is taxable service and hence interest of Rs.50,000/- (L) is included in the denominator.
- Inputs services exclusively used for taxable activities (IST) are not considered for reversal as the same falls under Rule 6(2) and not Rule 6(3).
- Services specified under Rule 6(5) (ISS) are not considered for reversal as per Circular No. 868/6/2008-CX dated 09-05-2008.
- Trading is not treated as exempt goods or exempt services.

23 Cenvat credit attributable to trading activity

Cenvat credit of Input Services attributable to trading is an issue for an assessee who is service provider as well as trader. Whether service provider can claim full Cenvat in respect of common input services used for trading and service provision is a vexed issue. Provider of taxable service and exempted service (not maintaining separate accounts) is required to reverse the common input services pertaining to exempted / non taxable service. Whether trading is service? If answer is no, then trading can not be regarded as exempt or non-taxable service. Ahmedabad CESTAT in the stay application of Orion Appliances Private Limited [2009-TIOL-1285] held as under:

- Trading activity can not be called a service and, therefore, it can not be considered as an exempted service also.
- Rule 6(3) applies to a person providing taxable and exempt services. Trading not being an exempt service, it is not correct to apply this rule.
- Trading is an activity which is neither manufacturing nor service and hence trader is not eligible for Cenvat credit.
- Appellant should segregate the quantum of input services attributable to trading and exclude it from Cenvat availment.

24 **Conclusion:**

An efficient tax credit mechanism is a key to the success of any value added tax system. Approach of tax payers is to claim each and every input tax credit whether eligible or not. Department take an extra cautious approach while allowing any tax credit. This conflict of approach has made Cenvat credit a highly litigative issue. Cenvat Credit Rules, 2004 is a complicated piece of legislation. The law is still developing and maturing on this subject. The discussion and deliberation on this subject is never ending. The author concludes here with sincere hope that this article will help readers to get some clarity on this complicated subject.