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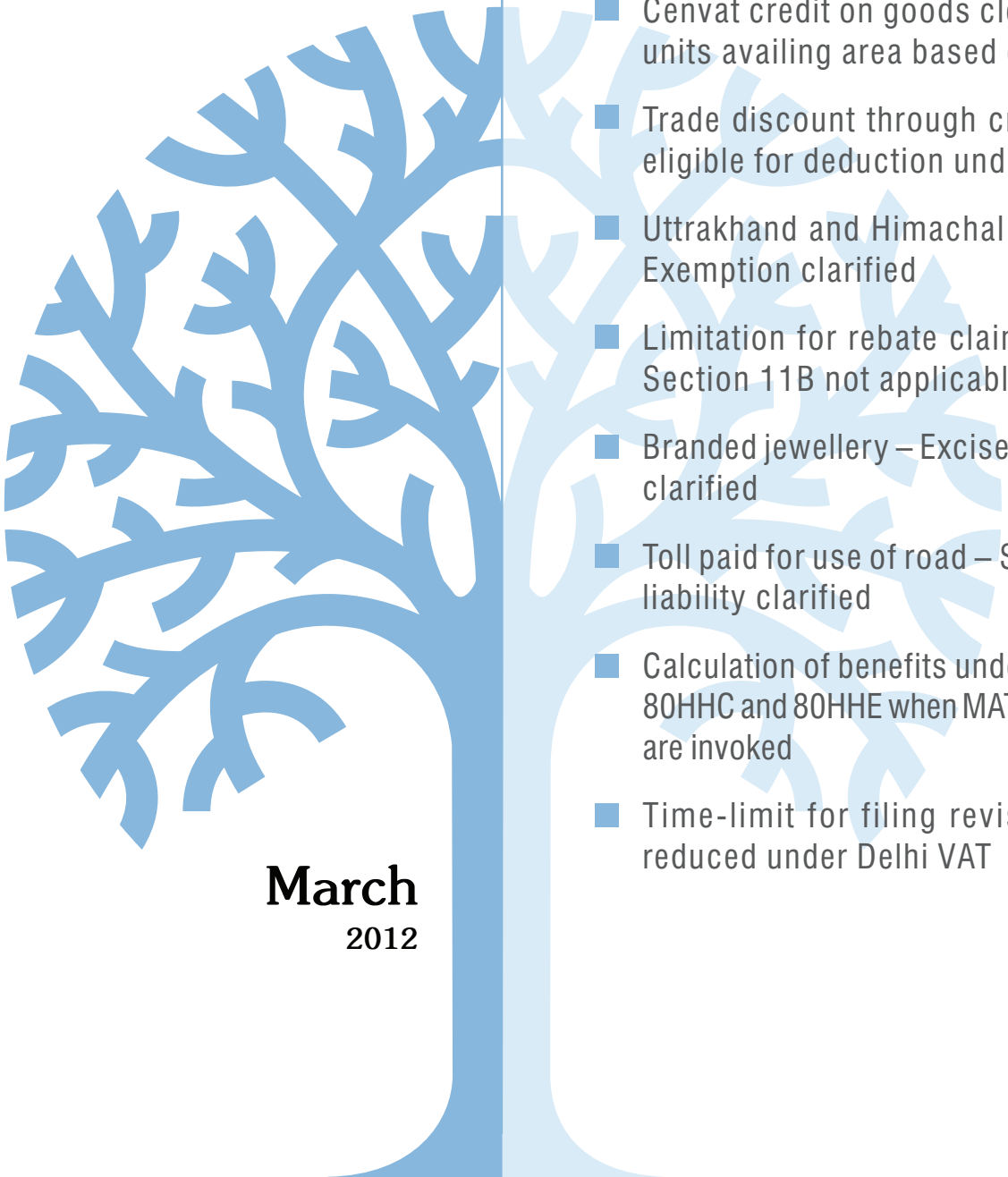
In Focus



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Budget 2012 – Let the credit flow

By **G. Gokul Kishore**

A budget presents a wonderful set of paradoxes. Things constant and eternal on the one hand and those with absolute caprice on the other mark all annual financial statements. The first category includes pre-budget memoranda, particular prayers, post-budget comments according to the side of the political spectrum one is and the like. A rate change, an exemption, a benefit – all of them come under the capricious category. Budget 2012 has been, so far, very compliant with this 'template'. A hike in excise duty rate as part of rollback of 2008 stimulus package, introduction of a negative list for services, introduction of DTC-related provisions like GAAR and CFC and some major relief for the salaried are giving some breathless moments to sectors likely to be impacted by such measures, if implemented. Leaving speculative elements aside, this article would like to take a brief tour of certain issues on the Cenvat credit side which hopefully the FM will address in this year's budget.

Ever since the eighties when Modvat credit became part of the rule book, reams of paper have been spent on clarifying, explaining, interpreting and re-writing Cenvat credit provisions. While more than two decades of operating the scheme can be perceived as helpful to the administration in ironing out the issues and fine-tuning the scheme, unfortunately, every round of liberalisation has been accompanied by fresh bout of divergence and conflict between the tax payer and the tax collector. This budget will be remembered for right reasons if the Cenvat credit availability on capital goods is not restricted during first year and the trade is allowed 100% credit on receipt of the goods.

Since 2004, Cenvat credit on input services has dominated both compliance and litigation spheres. A major reform with sufficient farsightedness and reasonable large heartedness by innovative solutions like the one 'in or in relation to manufacture of final product' which was a major step forward in respect of credit on inputs, can help. May be, 'in or in relation to manufacture and / or providing taxable services' is a solution but legal pundits need to come up with an out-of-the-box solution for input services keeping in mind the fact that the expression 'activities related to business' was not of much assistance to anybody.

A related issue on Cenvat credit is payment of interest when credit taken has not been utilised. The situation arising out of Apex Court ruling [*UOI* v. *Ind-Swift Laboratories* – 2011 (265) E.L.T. 3 (S.C.)] needs to taken into account by the tax administration. The legislative intention cannot obviously contradict commercial or accounting norms. Interest liability does not arise when no amount is enjoyed or taken advantage of. An atmosphere of trust can be fostered if the provisions are re-cast to clearly rule out interest liability on mere entry in the books, of an amount representing Cenvat credit.

Continuing with credit issues, one would expect Service Tax on freight paid as credit to manufacturers and service providers. Hair-splitting contentions on 'upto place of removal' and 'from the place of removal' are exercises which benefit neither the exchequer nor the assessee. Freight and a tax on freight are costs and the administration on the threshold of full-fledged value added tax in the form of GST, needs to extend credit without tying it with factory gate or port of export.

While explaining last year's budget amendments, the C.B.E. & C. by its circular dated 29-4-2011 clarified the expression 'any goods which have no relationship whatsoever with the manufacture of a final product' [which appears in Rule 2(k) on eligible inputs to exclude items] whereby it stated that goods such as furniture and stationery used in an office within the factory are goods used in the factory and are used in relation to the 'manufacturing business' and hence the credit of same is allowed. If credit can be extended to stationery and furniture, there cannot be any argument over credit of tax paid on GTA service. One can also add construction services used by manufacturers and service providers to this wish-list which like the issues surrounding credit, is endless. For once, let us retain optimism and wait till 16th March, 2012.

[The author is Senior Manager, Lakshmikumaran & Sridharan, New Delhi]

CUSTOMS

Notifications & Circulars

Equipments for ITER project and LR-SAM programme, exempted : Government of India has, by two independent notifications, granted exemption from customs duty and additional customs duty (CVD & SAD) on import of machinery, equipments, etc required for the International Thermonuclear Experimental Reactor-India (ITER-India) project of the Department of Atomic Energy as well as the Long Range-Surface to Air Missile (LR-SAM) Programme of the Ministry of Defence. Notifications No. 5/2012-Cus., dated 7-2-2012 and No. 6/2012-Cus., dated 9-2-2012 issued in this regard amend Notification No. 39/96-Cus. and prescribe the conditions to be fulfilled to avail such exemption.

Iron content in iron ore - Procedure for calculation of: C.B.E. & C. has issued Circular No. 4/2012-Cus., dated 17-2-2012 to provide for uniform practice for calculation of iron content in iron ore for the purpose of charging export duty. It has been clarified that Fe content shall be calculated based on Wet Metric Ton (WMT) which in other words means deducting the weight of impurities (inclusive of moisture) out of the total weight/gross weight to arrive at Net Fe content. Currently, ports follow either the Dry Metric Ton (DMT) method or the Wet Metric Ton (WMT) method.

Cotton exports prohibited: India has prohibited export of cotton - carded or combed and neither carded nor combed (Tariff Headings 5201, 5203). DGFT Notification No. 102, dated 5-3-2012 also prohibits exports under registration certificates already issued and further states that the transitional arrangements as available in para 1.5 of FTP will also be not applicable. In this connection, C.B.E. & C. has also issued Circular No. 6/2012-Cus.

Detention by Customs – Importers/exporters to be advised to warehouse goods: The Central Board of Excise & Customs has instructed its field formations to give option to importers/exporters to keep the goods in warehouses where release of goods even on provisional basis is not possible. Instruction No. 450/160/2011-Cus.IV, dated 13-2-2012 states that detention by Customs in routine disputes or without valid grounds causing demurrages would be viewed seriously.

Ratio decidendi

Customs cannot be burdened with demurrage for failure of importer to take delivery of the goods: Delhi High Court has recently held that exemption from demurrage cannot be claimed by an assessee when they had failed to take delivery of goods. The assessee had

filed a petition before the Delhi High Court seeking release of goods without payment of demurrage and detention charges consequent to favorable order by CESTAT. The High Court had earlier ordered for release of goods on execution of PD bond, and the Customs officers had also issued detention certificate but the assessee/petitioner had failed to take delivery of the goods [*Monika India* v. *Union of India* - 2012-TIOL-169-HC-Del].

Exemption deniable if Country of Origin misdeclared: Exemption is deniable when goods were mis-declared as to country of origin. In the case before CESTAT, goods were imported by claiming exemption under Notification No 73/2005-Cus (India-Singapore Free Trade Agreement). The country of origin was mis-declared as Singapore, whereas in fact the goods were actually obtained from Taiwan and Korea. Though the appellants contended that they were not party to the fraud as they were not aware of the tainted nature of the certificate of the origin, the CESTAT while denying the exemption, upheld the order of duty demand, interest and penalty [*Jensons Industries* v. *Commissioner* - 2012-TIOL-269-CESTAT-Ahm].

CENTRAL EXCISE

Notifications & Circulars

Specified missile development programme – Exemption granted again: Exemption has been granted to machinery, equipments, instruments, etc. required and cleared for Long Range Surface to Air Missile (LR-SAM) Programme of Ministry of Defence. The exemption earlier available till 24-11-2011 has been now provided by Notification No. 4/2012-C.E., dated 9-3-2012 till 24-5-2012.

Cenvat credit on goods cleared from units availing area based exemption: Rule 12 of the Cenvat Credit Rules, 2004 has been amended to provide for restrictions as given in the proviso to Rule 3(1)(i) in respect of availability of Cenvat credit to units getting inputs or capital goods from units located in specified areas in Kutch, J&K & North Eastern Region. Now such recipient units would not be allowed to take credit if the unit in the specified areas had paid the duty using Notification No. 1/2011-C.E. Prior to the aforesaid amendment by Notification No. 1/2012-C.E. (N.T.), dated 9-2-2012, Rule 12 was having overriding effect vis-à-vis other provisions of Cenvat Credit Rules.

Rebate on excisable goods used in goods exported to Nepal: Exports to Nepal have been made on par with exports to any country other than Bhutan with effect from 1-3-2012 as per amendments made by notifications issued in December last year. Now, Notification No. 21/2004-C.E. (N.T.), dated 6-9-2004 providing for rebate of duty on excisable goods used in goods exported has been amended by Notification No. 2/2012-C.E. (N.T.), dated 22-2-2012 to include Nepal exports also and the same is also effective from 1-3-2012.

Uttrakhand and Himachal Pradesh – Exemption clarified: Exemption to units situated in Uttarakhand and Himachal Pradesh is available under Notifications No. 49/2003-C.E. & No. 50/2003-C.E. even in situations where there is a change in the ownership of an existing unit, where the existing unit is shifted within the notified areas in a State and where an existing unit acquires an adjacent land and installs fresh plant & machinery there. C.B.E.& C. Circular No. 960/3/2012-C.E., dated 17-2-2012 has been issued in this regard.

Branded jewellery – Excise exemption clarified: Central Excise duty is leviable on precious metal jewellery, manufactured or sold under a brand name, only if the trade/brand name is indelibly marked or embossed on such jewellery. As per latest clarification issued from file F.No. 354/38/2011-TRU, dated 2-3-2012 by C.B.E. & C., if the brand name is not affixed or embossed on the jewellery or article itself but appears

on the packing such as the jewellery box or pouch or on the warranty card or certificate of quality, such goods will not be treated as branded jewellery and thus will not be liable to excise duty.

Ratio decidendi

Limitation for rebate claim – Section 11B not applicable: The Madras High Court has held that limitation under Section 11B of the Central Excise Act, 1944 will not apply to rebate claims made under Rule 18 of the Central Excise Rules, 2002. While coming to the said conclusion, the court compared the existing and the predecessor notifications issued under Rule 18 ibid. It noted that while the predecessor notification specifically borrowed the time limit mentioned under Section 11B, the present notification issued under said rule i.e. Notification No. 19/2004-C.E. (N.T.) did not prescribe any time limit [*Dorcas Market Makers Pvt. Ltd.* v. *Commissioner* - 2012-TIOL-108-HC-CX].

Valuation in case of job work: In a recent decision, the Supreme Court has remanded the case before it to the Tribunal on the ground that the Tribunal did not address or analyse the nature of relationship between the job worker and the company and did not determine whether both the parties were related or not. It has asked the Tribunal to consider whether the relationship between the assessee-jobworker and the principal was that of a related person. The Department had contended that the nature of relationship between the job-worker and the company was not on principal to principal basis and hence the valuation should have been done based on sale price of the principal. It was also held that if the Tribunal came to the conclusion that both the parties were not related, then valuation method adopted by the assessee would hold good. It should be noted that the aforesaid judgment was rendered for the period before the introduction of Rule 10A of the Central Excise (Determination of Price of Excisable Goods) Rules, 2000 [*Commissioner* v. *Food & Healthcare Specialities* - 2012-TIOL-14-SC-CX].

Kutch exemption not admissible to goods produced using machinery installed after cut-off date: Customs, Excise and Service Tax Appellate Tribunal has held that once the benefit of relevant notification was available only to goods produced from investments made till 31-12-2005, the benefit could not have been made available to goods produced from the investments made after the cut-off date irrespective of the fact that such investments were made in the existing unit. In this case, the assessee started its unit in Kutch and was availing benefit of exemption under Notification No. 39/2001-C.E. which is available to units whose investments were complete by 31-12-2005. The assessee set up new plant and machinery in its unit post 31-12-2005 and contended that it was eligible for exemption for the goods produced from the new plant and machinery also [*Ratnamani Metals and Tubes Ltd.* v. *Commissioner* - 2012 (276) ELT 230 (Tri.-Ahmd.)].

Slagwool and Rockwool – Classification of: The Supreme Court of India has held that rock wool and slagwool manufactured using 25% (by weight) of blast furnace slag is rightly classifiable under sub-heading 6807 10 of the Central Excise Tariff. The department had contended that the said goods were classifiable under Heading 6803 ibid. covering slagwool, rockwool & similar wools and having higher rate of duty. The court noted there was no dispute that the goods were manufactured using more than 25% by weight of red mud, press mud or blast furnace slag or one or more of these materials. The Department had relied on circular dated 17-9-2001 wherein the traders dealing in rockwool and slagwool, had specifically classified the said goods under Heading 6803. The Court also observed that in a classification dispute, an entry beneficial to the assessee is required to be applied. It was also noted that the departmental circulars are not binding on assessee or quasi judicial authorities or courts [*Commissioner* v. *Minwool Rock Fibres Ltd.* - 2012-TIOL-18-SC-CX].

SERVICE TAX

Circular

Toll paid for use of road – Service Tax liability clarified: Service Tax is not leviable on toll fee paid by the users of roads, including those roads constructed by a Special Purpose Vehicle (SPV) by contract between NHAI/State authority and concessionaire. Circular No. 152/3/2012-S.T., dated 22-2-2012 issued in this regard states that if the SPV engages an independent entity to collect toll fee from users on its behalf, Service Tax liability would arise under the 'Business Auxiliary Service' on commission or charges paid to such entity. Further, as per the circular, leasing, or licensing of vacant land by NHAI/State authorities to an SPV for construction of road as also such construction will not attract Service Tax.

Ratio decidendi

Cenvat credit to service providers: CESTAT in its recent order has denied Cenvat credit on tower and tower parts, pre-fabricated building and green shelter, printer and office chair to the assessee engaged in providing telecommunication service. The Tribunal considered the definition of capital goods and held that towers or parts thereof are not components of antennas as a component has to be a constituent part, which was not the case before it. It was held that towers, being gigantic immovable structures, cannot also be said to be accessories of antennas. The Tribunal also analyzed Explanation 2 of the definition of inputs which includes inputs used in the manufacture of capital goods which are further used in the factory of manufacturer and held that the said explanation was specifically applicable to manufacturer and cannot be extended to service provider. Extending the aforesaid, credit was rejected on pre-fabricated building and green shelter and chairs also. Cenvat credit on printer was denied on the ground that it was an equipment used in office [*Bharti Airtel Ltd.* v. *Commissioner* - 2012-TIOL-209-CESTAT-Mum].

Bank run by Co-operative society liable under Banking and Financial services: The CESTAT has held that the assessee-co-operative society, providing banking services would be liable to Service Tax under Banking and Other Financial Services. The assessee had contended that a co-operative society cannot be considered as a body corporate in terms of specific exclusion from the definition of the term under the Companies Act, 1956 and that due to such exclusion, it could not be included in the expression "any other person". Rejecting this contention, the Tribunal held that even if a co-operative society was excluded from the purview of body corporate, it was for a limited purpose to exempt the same from the elaborate procedures of the Companies Act. The Tribunal thus concluded that the assessee was covered under the expression "any other person" and was liable to pay Service Tax [*Madhav Nagrik Sahkari Bank Ltd.* v. *Commissioner* - 2012-TIOL-234-CESTAT-Del.].

VALUE ADDED TAX (VAT)

Notification

Time-limit for filing revised return reduced under Delhi VAT: Section 28 of the Delhi VAT Act deals with correction of deficiencies in the return and provides a time-limit of four years to file revised return and pay short paid tax in case of mistake or error in the return. This time-limit has been substituted with 'the next financial year' by Delhi Value Added Tax (Amendment) Act, 2012, thereby reducing the time limit for correcting deficiencies in the return.

Ratio decidendi

Utensils to cover items used for preparing, serving or keeping food or beverages: The Madhya Pradesh High Court in its recent order has held that in common parlance utensils mean items of daily household use generally used for preparing, serving or keeping food or beverages. The matter was for classification of plastic and steel items like water jug, bottles, lunch box, stainless steel flask, tray, dry fruit box, etc. under the Madhya Pradesh VAT Act. The Commissioner had, in his order, held that only water jug was covered within the meaning of 'utensils' in Entry 6, Part II of Schedule II of the Act taxable at 5%. The remaining items according to the Commissioner were covered under Entry 1, Part IV of Schedule II attracting the levy of tax at 13%. The order passed by the Commissioner restricting the meaning of utensils to only the items used in the kitchen, was set aside and the matter was remanded back to him for deciding the petitioner's application afresh in the light of the observation made by the court [*P.K Plastics* v. *Commissioner of Commercial Tax* - 2012 VIL 20 M.P.]

Trade discount through credit notes eligible for deduction: The Supreme Court has held that a discount is allowable subject to two conditions namely, the discount is given in accordance with the regular practice in the trade and second, the accounts should show that the purchaser has paid only the sum originally charged less the discount. The issue which came up for determination was whether the trade discounts given through credit notes qualify as discounts and are eligible for deduction under Rule 9(a) (which provides for determination of taxable turnover) of the Kerala General Sales Tax Rules. The Kerala High Court had held that unless the discount was shown in the invoice itself, it would not qualify for deduction and further any discount that was given by means of credit note issued subsequent to the sale of the article was in reality an incentive and not trade discount eligible for deduction under Rule 9(a). The Supreme Court while relying on various judgments which allowed the deduction of trade discounts to compute the taxable value set aside the ruling of the Kerala High Court and observed that Rule 9(a) does not speak of invoices but stipulates that the discount must be shown in the accounts. The assessee had a scheme of trade discount for its dealers under which the dealer on achieving a pre-set sale target would be entitled to certain discount on the price [*IFB Industries Ltd.* v. *State of Kerala* - 2012-VIL-04-SC].

INCOME TAX

Ratio decidendi

Netting of income from expenditure allowed for Explanation (baa) to S. 80HHC: The AO & CIT(A) computed Section 80HHC deduction by deducting 90% of the gross interest received from the profits of business. However, the Tribunal held that only the net interest could be deducted (subject to nexus between the expenditure and income being proved). On appeal by the department, the High Court reversed the Tribunal's decision and held that the gross receipts had to be excluded. The Supreme Court held that under Clause (1) of Explanation (baa) to Section 80HHC, 90% of any receipts by way of brokerage, commission, etc., included in any such profits have to be deducted from the profits & gains of business. The expression "included in any such profits" means such receipts by

way of brokerage, commission, etc included in the profits & gains. Therefore, if any quantum of receipts by way of brokerage, commission, etc is allowed as expenses u/s 30 to 44D and is not included in the profits of business, 90% of such quantum of receipts cannot be reduced under clause (1) of Explanation (baa) to Section 80HHC. In other words, only 90% of the net amount of any receipt of the nature mentioned in clause (1) which is actually included in the profits of the assessee is to be deducted from the profits of the assessee for determining "profits of the business". [*ACG Associated Capsules Pvt. Ltd* v. *CIT – C.A. No. 1914 of 2012 - Supreme Court order dated 8-2-2012*]

Cost of acquisition and indexation of capital asset sold by a trust: The assessee had acquired a property prior to 1st of April, 1981 and transferred it to a trust on 5th of January, 1996. The Delhi High Court rejected the contention of the Department and held that the assessee was entitled to the benefit of the indexed cost of acquisition from 1-4-1981 and not 5-1-1996. Cost of acquisition should be the cost to its previous owner and should be indexed from the year of acquisition by the previous owner and not the trust as contended by the Department. [*Arun Shungloo Trust* v. *CIT - ITA 116/2011 & Order dated 13-2-2012*]

Calculation of benefits under Sections 80HHC and 80HHE when MAT provisions are invoked: The assessee in this case claimed a deduction of Rs. 1, 56, 33,719/- against net profit as per profit and loss account amounting to Rs. 3, 07, 84,105/- to arrive at book profit of Rs. 1,51,50,386/- under Section 115JA of the Income Tax Act, 1961.The assessing authority however denied the benefit of Section 80HHE on the ground that after set off of brought forward losses there would be no net profit left against which the assessee could claim benefit of Section 80HHE. The Supreme Court while affirming the judgement of High Court held that once the law itself declares that the adjusted book profit is amenable for further deductions on specified grounds, in a case where Section 80HHC /80HHE is operational it becomes clear that computation for the deduction under those sections needs to be worked out on the basis of adjusted book profits and not on the basis of the profits computed under the regular provisions of law applicable to computation of profits and gains of business. [*CIT* v. *Bhari Information Tech Sys. P. Ltd. - C.A. No. 33750/2009*]