

For Official Use Only



Government of India

MONTHLY AUDIT BULLETIN – OCTOBER, 2014

**Directorate General of Audit
Customs & Central Excise
Central Revenue Building,
I.P. Estate,
New Delhi-110109**

INDEX

S.No.	Topic	Page No.
CENTRAL EXCISE		
1.	Non Payment of amount equal to 6% of the value of emptied goods	2
2.	Irregular availment of Cenvat Credit on packing material not used within the factory	4
3.	Non payment of Central Excise duty for clearance under EPCG License	5
4.	Non payment of Central Excise Duty on VAT remission	6
5.	Non payment of Central Excise Duty resulting from Non-inclusion of value of Free-issue materials consumed in the manufacture of excisable goods by the assessee	7
6.	Irregular availment of Exemption under Notification No. 12/2012 for clearance of Solar Inverters, Array Guard/Combiner Box, PV logs.	8
SERVICE TAX		
7.	Non-payment of service tax on land lease rentals Received	9
8.	Short payment of Service Tax in respect of import of Consulting Engineering Service.	10
9.	Incorrect Computation of Taxable Value of Services on Account of Reimbursable Expenses made to Foreign Establishment located in Non-Taxable Territory	11
10.	Wrong availment of Exemption Notification	12
11.	Non Payment of Service Tax	13
12.	Non Payment of Service Tax on R & D services Performed	14

MONTHLY AUDIT BULLETIN – OCTOBER, 2014

CENTRAL EXCISE

1. **GIST OF THE OBJECTION** : Non Payment of amount equal to 6% of the value of exempted goods i.e. Electricity in terms of Provisions of Rules 6(3) of Cenvat Credit Rules, 2004.

COMMISSIONERATE : Central Excise Commissionerate, Meerut

CONTRAVENTION OF PROVISION : Sub-rule 3 of rule 6 of the CENVAT Credit Rules, 2004

AUDIT CODE : CE-/R04

During the course of audit it has been observed that the assessee is engaged in the production of electricity i.e. exempted goods. As per Board Circular No. 904/24/2009-CX dated 28.10.2009, it was clarified that with the amendment in clause (d) of Section 2 of CEA, 1944, the Baggage, aluminium/Zinc dross and other such products termed as waste, residue of refuse which arise during the course of manufacture and are capable of being sold for consideration would be Excisable goods and chargeable to payment of Excise duty. It was further clarified that in case of rate of duty in respect of such products is NIL in the Tariff or they are exempt from duty in term of any exemption notification, and if Cenvat credit has been taken on the inputs which are used for dutiable and exempted goods, then in terms of Rule 6 of CCR, 2004, the Assessee is required to reverse the proportionate credit of pay 6% amount.

During the course of audit of assessee, it was observed that they, apart from clearing dutiable goods of the party are also clearing Baggase and also using baggase captively for generation of electricity. Baggase cleared captively was capable of being sold for consideration. Rule 6 (2) of CCR, 2004 provides that a manufacturer or provider of output service who avails of Cenvat Credit on common input or inputs services and manufactures both dutiable and exempted goods or provides exempted services, then he has to maintain separate accounts of receipt & issue of input/services for both category of final products/services. However, if the manufacturer opts not to maintain separate accounts, then he shall pay an amount equal to 6% of the value of the exempted goods and exempted Services of pay duty by exercising option under Sub Rule 3A of rule 6 *ibid*. In the instant case, the party is availing Cenvat Credit on common input/input services in the manufacture of dutiable goods from the party, but they did not maintain separate accounts of receipt & use of inputs/input Services in respect of exempted goods, i.e. Baggase. As such, they were liable to pay an amount equal to 6% of value of clearances of Baggase in terms of provisions of Rule 6 (3) of CCR, 2004 read with above Board Circulars. The baggase was used captively for production of electricity which is an exempted goods falling under Chapter Heading No. 27160000 of CETA, and part of electricity so generated was either used within the factory for the production of goods or sold to others. The party was liable to pay an amount equal to 6% of the sale value of the Electricity sold to other Party which is Rs. 5,65,26,311/- for the period from February 2014 to March 2014 in terms of provision of Rule 6 (3) of CCR, 2004 and an amount equal to 6% of value comes to Rs. 33,91,579/- and the same is recoverable from them alongwith interest. On being pointing out the fact party has submitted that they will contest the issue.

2. **GIST OF THE OBJECTION** : Irregular availment of Cenvat Credit on packing material not used within the factory.

COMMISSIONERATE : Central Excise Commissionerate, Tirupati

CONTRAVENTION OF PROVISION : Rule 4(1) of CENVAT Credit Rules, 2004

AUDIT CODE : CE-IR010

The assesseees are manufacturers of Sugar falling under Chapter 17 of the CETA 1985. They are purchasing Laminated pouches/ Film rolls falling under Chapter 39, from various buyers, for packing sugar. Those goods are consigned for delivery at the place of packaging the said goods i.e., M/s. Santoshi Mata Oil Packing Industries Ltd, M/s. Balaji Foods Vijayawada, M/s. Venkata Rakesh Trading Co., Vijayawada, mentioning consignee as "M/s. Sudalagunta sugars Ltd". The assesseees are clearing Sugar to the aforesaid packing premises, on payment of applicable duty, mentioning on the Central Excise invoice as "Self-PDS Sugar Packing Unit, A/c. the assessee name".

It was noticed that the assessee availed Cenvat Credit on the said packing material, which were not received in the factory of manufacture and were used for packing the finished goods at the premises of the packing unit. The audit pointed out that as per **Rule 2** of Cenvat Credit Rules, 2004, 'input' means **all goods used in the factory by manufacturer of final products** and as per **Rule 4(1)** *ibid*, the **Cenvat Credit in respect of inputs may be taken immediately on receipt of inputs in the factory of manufacturer**. In the instant case, the inputs were not received in the factory of manufacture and they were used for packing the goods (which were already cleared under an invoice) at the premises of the packaging unit. Hence, the credit availed on the packing material was irregular. On being pointed out the assessee agreed to the objection and reversed / paid the credit of Rs. 134.73 lakhs, so availed irregularly and also paid interest of Rs. 30,148/-.

3. GIST OF THE OBJECTION : Non payment of Central Excise duty for clearance under EPCG License (Terminal Excise Duty).

COMMISSIONERATE : Central Excise Commissionerate, Vapi

CONTRAVENTION OF PROVISION : Goods cleared without payment of duty, section 11A of the Central Excise Act, 1994.

AUDIT CODE : CE-CR040

The assessee is engaged in manufacturing of Kool Glass, Solid Glass, EDGE worked glass etc. classifying the same under Chapter Heading No. 70 of the CETA, 1985.

During the course of audit, while scrutinizing the financial records of the said assessee, i.e. Balance sheet and ledger thereof, it was observed that the assessee has shown certain amount of excise duty payable by them. On being inquired, they informed that they had cleared goods under various invoices for the period from 23.05.2010 to 18.07.2012 under EPCG license issued to the customer without payment of Central Excise Duty. As per the EPCG scheme, the goods can be procured by the license holder without payment of duty however, the supplier has to clear the goods on payment of duty and then they can claim the said Terminal Excise Duty as refund on the basis of end user's certificate. Hence, the clearance made by the assessee without payment is totally incorrect and they are required to pay the duty involved in such clearances.

On being inquired, the assessee stated that they had already paid the duty to the tune of Rs. 5,35,037/- on 14.03.2013 out of total duty involved to the tune of Rs. 37,51,150/-. Hence, the remaining duty to the tune of Rs. 32,16,113/- is required to be recovered from the assessee along with interest.

4. **GIST OF THE OBJECTION** : Non payment of Central Excise Duty on VAT remission.

COMMISSIONERATE : Central Excise Commissionerate,
Guwahati

CONTRAVENTION OF PROVISION : Under Valuation Section 4(3)(d) of Central Excise Act, 1994.

AUDIT CODE : CE-VR070

While scrutinizing the record during audit, it is noticed that the assessee have been availing VAT remission for their sales. On examination of records during audit, it has been observed that the said assessee had charged and realised Assam VAT from their buyers for sales under Assam Value Added Tax Act, 1993. On further scrutiny, it is also seen that the said assessee had availed VAT Remission of 99% under The Assam Industries (Tax Exemption) Scheme, 2009. In other words only 1% of the amount of VAT so collected from buyers is paid to state government and remaining 99% is retained by the said assessee as remission under The Assam Industries (Tax Exemption) Scheme, 2009. As per Section 4, Sub-Section 3(d) of the Central Excise Act, 1944, the 'transaction Value' excludes the amount of duty of excise, sales tax and other taxes, if any, **actually paid or payable** on such goods. Further, in terms of CBEC Circular No. 880/18/2008-CX dated 22.12.2008 and F.No. 354/81/2000-TRU dated 30.06.2000, (issued in the context of J & K Govt. on similar issue) the amount of VAT collected from buyers and not paid to the state (remitted by State) is includible in the assessable value for the purpose of charging Excise Duty. Therefore, it has resulted in short payment of duty on the amount enjoyed by the said assessee as remission of VAT. During the period from April, 2012 to March, 2014, the assessee had received total amount of Rs. 5,59,27,270/- as VAT Remission for the goods cleared by them under Section 4 of the Central Excise Act, 1944. Hence, Central Excise Duty total amounting to **Rs. 69,12,612/-** (BED Rs. 67,11,274/- + EC Rs. 1,34,225/- + SHEC Rs. 67,113/-) is recoverable from them. They were, therefore, required to pay an amount of Rs. 69,12,612/- along with appropriate interest as applicable.

5. GIST OF THE OBJECTION : Non payment of Central Excise Duty resulting from Non-inclusion of value of Free-issue materials consumed in the manufacture of excisable goods by the assessee.

COMMISSIONERATE : Central Excise Commissionerate, Kolkata VII

CONTRAVENTION OF PROVISION : Section 4 of Central Excise Act, 1994.

AUDIT CODE : CE-VR060

The assessee are engaged in the manufacture of '**Transformer & Components**' falling under CETH No. 85049010, 'Vacuum Circuit Breaker' falling under CETH No. 85352121, 'Switchgear Components' falling under CETH No. 85381010 & 'Motor Components' falling under CETH No. 85030029 of Central Excise Tariff Act, 1985. Scrutiny of records viz Purchase orders, invoices etc. relating to manufacture & clearance of the said items revealed that certain materials, supplied free of cost by four buyers were consumed in the manufacture of the said excisable goods (for the sake of brevity- the 'said goods') as per specifications mentioned in respective purchase orders but the assessable value of the said goods, for which the free issue material were essential components/ ingredients, were not included in the value of such free issue materials as is evident from relevant invoices for clearance of the said goods. On scrutiny of such Invoices it has been observed that the value of the free issue material, consumed for respective items of the said goods were taken into consideration for arriving at assessable value of the said goods but while determining the value for the purpose of assessment to Central Excise duty of the said goods, the value of requisite quantity (-ies) of free issue materials was deducted from such assessable value mentioned above and C. Ex. Duty has been paid on such lower value. As the free issue materials mentioned above form an integral component of the finished excisable goods manufactured strictly in terms of the respective buyers P. Os, its value also forms part of the intrinsic value of the finished excisable goods in which the free issue materials is contained requiring its (-of the free issue material's) value to be taken into consideration for assessment to C. Ex. Duty under Section 4 of the Central Excise Act 1944. In view of above, there has been undervaluation of goods resulting in short payment duty of Rs. 44,19,948/- (**Incl. Cess**) which is recoverable from the assessee along with interest.

6. **GIST OF THE OBJECTION:** Irregular availment of Exemption under Notification No. 12/2012 for clearance of Solar Inverters, Array Guard/Combiner Box, PV logs.

COMMISSIONERATE : Central Excise Commissionerate,
Bangalore III

CONTRAVENTION OF PROVISION : Without Payment of duty section 11A of the Central Excise Act, 1994.

AUDIT CODE : CE-CR020

During the verification of Central Excise records of the assessee, it is noticed that the assessee have availed exemption under Notification No. 12/2012 CE dated 17.03.2012 (Sr. No. 332, List 8, No. 10, on Solar Inverters falling under TSH 85044010, Combiner Box/Array Guard falling under TSH 85049090 and PV Logs falling under TSH 85371000, by claiming the said items as "Solar Power Generating System" and cleared the said goods without payment of duty. On perusal of List 8 Sr. No. 10 of the said Notification, it appears that the exemption is not available for Solar Inverters, Combiner Box/Array Guard, PV Logs etc., in as much as they are not "Solar Power Generating System". The total value of Solar inverters, Array Guard/Combiner Box, PV Logs cleared from Dec. 2011 to June 2014 is Rs. 84,66,27,597/- and the total duty involved is Rs. 10,00,32,771/-. Solar Power Generating System consists of Photo Voltaic modules and Cells, Inverters and various other components, when put together becomes Solar Power Generating System and Photo Voltaic modules/Cells, Inverters and Switch boxes and other components are individual components/devices and not a System and these parts/components are not mentioned in the list 8 and hence are not eligible for the exemption under Sr. No. 332 of Notification 12/2012 CE dated 17.03.2012 as claimed by the assessee. The assessee reversed the amount of Rs. 10,00,32,771/- in their Cenvat account under protest and requested for Show Cause Notice/Speaking Order. In the AMC it was decided that to take appropriate action for vacating the protest and for recovering interest and penalty.

SERVICE TAX OBJECTIONS:

OBJECTION NO. 1

GIST OF THE OBJECTION : Non-payment of service tax on land lease rentals Received.

COMMISSIONERATE : Service Tax Commissionerate, Visakhapatnam I.

CONTRAVENTION OF PROVISION : Section 68 of the Finance Act, 1994.

AUDIT CODE : ST-CSR012

The tax payers are providers of port services. The audit noticed that commencing from 2001 onwards, the tax payers were leasing out vast tracks of land in their possession to various parties for their commercial use on long lease and received certain amounts as upfront payments. However, they are amortizing the amounts so received in their books of accounts on yearly basis. The audit noticed that with the expansion of scope of definition of 'Renting of immovable property services' w.e.f. 01.06.2007, brought about by Finance Bill 2010, the Service Tax on renting of vacant lands came in to effect from 01.07.2010.

The audit noticed that the tax payers did not pay service tax on amounts received towards land lease rentals. On enquiry, it was informed that the tax payers received most of their land lease rental amounts prior to July 2010, i.e., before introduction of service tax on renting of vacant lands. The audit studied Notification No. 36/2010-ST dated 28.06.2010 and observed that 'advance payments' received prior to 01.07.2010, in respect of eight new services and other activities brought into service tax net on account of expansion of scope of existing services were exempted, with the exception of 'commercial training or coaching services and renting of immovable property services'. The audit pointed out that the tax payers are, therefore, liable to pay service tax of Rs. 35.58 crores on a taxable value of Rs. 344.18 crores. The assessee agreed to the objection and paid Rs.26 crores. The balance amount of Rs.9.58 crores has to be recovered along with interest and penalty.

OBJECTION NO. 2

GIST OF THE OBJECTION : Short payment of Service Tax in respect of import of Consulting Engineering Service.

COMMISSIONERATE : LTU, Delhi.

CONTRAVENTION OF PROVISION : Section 68 of the Finance Act, 1994.

AUDIT CODE : ST-VSR010

During the course of audit of the assessee, it was observed that the party has been receiving Consultancy Services from abroad and was regularly discharging Service Tax liability under Reverse Charge Mechanism on payments made in foreign exchange. The party was also depositing the T.D.S. amount payable with Income Tax department on these foreign payments. In most of the cases, the amount of T.D.S. deposited was deducted from the payments made to the foreign service providers. However, in some cases, full payment of invoice amount has been made to the foreign service providers and while discharging the Service Tax liability, the amount of T.D.S. paid was not 'grossed up' with the payments made in foreign exchange.

The assessee agreed with the objection and deposited the Service Tax Rs. 29,26,876/-+Interest of Rs. 13,25,490/-.

OBJECTION NO. 3

GIST OF THE OBJECTION : Incorrect Computation of Taxable Value of Services on Account of Reimbursable Expenses made to Foreign Establishment located in Non-Taxable Territory.

COMMISSIONERATE : LTU, Delhi.

CONTRAVENTION OF PROVISION : Rule 5 (1) of Service Tax (Determination of Value) Rules, 2006.

AUDIT CODE : VSR07

The assessee is dealing in motor vehicle parts, while scrutiny of Balance Sheet and Profit and Loss Account of the party for the period 2012-13 and 2011-12, it was found that the party had made payment of reimbursable of expenses in Foreign Currency for an amount of Rs. 2,65,59,456/- and Rs. 1,37,40,908/- respectively as per agreement entered between them and their Holding company (foreign company) and various associated company on account of Technical Collaboration Agreement (IPR), Sub-License Agreement (IPR), ISIT Service Agreement (Business Auxiliary Services) and General Service Agreement. The party had paid Service Tax on the basic amount paid towards Trade Mark Fees (IPR), Royalty (IPR), ISIT (BAS) & GSA (BAS) but failed to discharge tax liability on the said reimbursable amount paid to Foreign Services Provider. Rule 5 (1) of Service Tax (Determination of Value) Rules, 2006 provides that where any expenditure or cost are incurred by the Service Provider in the course of providing taxable services, all such expenditure or cost shall be included in the value for the purpose of where any expenditure or cost are incurred by the Service Provider in the course of providing taxable services, all such expenditure or cost shall be included in the value for the purpose of discharging Service Tax on the said Services. Non-inclusion of those charges in gross amount having resulted into short payment of correct Service Tax. Since the Holding Company/Associated Company with whom the party has entered into agreement do not have their offices in India, the liability to pay service tax fall on the party under Reverse Charge Mechanism. Accordingly, the party are liable to pay Service Tax of Rs. 32,82,750/- including cess @ 12.36% and Rs. 14,15,315/- including cess @ 10.30% (total Rs. 46,98,065/-). They are also liable to pay interest and penalty as applicable.

OBJECTION NO. 4

GIST OF THE OBJECTION : Wrong availment of Exemption Notification
(Objection Code: CSR03).

COMMISSIONERATE : Service Tax, Kolkata.

**CONTRAVENTION
OF PROVISION** : Section 68 of the Finance Act, 1994.

AUDIT CODE : ST-CSR030

The assessee is a provider of 'Erection, Commissioning and Installation Services'. In the course of audit and on scrutiny of records, it has been observed by the auditors that they had availed exemption notification No. 04/2004-ST dated 31.03.2004 superseded by Notfn. No. 09/2009-ST dated 03.03.2009 (which is also amended by Notfn. No. 15/2009-ST dated 20.05.2009) for provision of service to SEZ Gross Taxable Value of exemption amounting to Rs. 4,91,15,,523/- in 2010-11, Rs. 2,47,43,693/- in 2011-12 and Rs. 5,29,37,421/- in 2012-13. It has been observed from the statement given by the assessee during Audit, that the assessee had provided services to the service receivers. Many of whom are not a Developer approved by the Board of Approvals or a unit of SEZ approved by the Developer Commissioner or Board of Approvals. The assessee with reference to audit query had admitted that they were sub-contractors and there is no provisions for exemption under the aforesaid notifications to the sub-contractors and it is clear that they had not provided any service to the developer directly as required under the conditions for claiming exemption for providing service to SEZ unit. Therefore, it appears that the assessee had wrongly availed exemption provided by Notification No. 04/2004-ST dated 31.03.2004 superseded by Notfn. No. 09/2009-ST dated 03.03.2009 (which is also amended by Notfn. No. 15/2009-ST dated 20.05.2009) and hence, they are liable to pay service tax of Rs. 50,58,899/- in 2010-11 and Rs. 25,48,600/- in 2011-12 @ 10.30% and Rs. 65,43,065/- in 2012-13 @ 12.36% plus interest and penalty as applicable.

OBJECTION NO. 5

GIST OF THE OBJECTION : Non Payment of Service Tax.

COMMISSIONERATE : Service Tax, Kolkata.

**CONTRAVENTION
OF PROVISION** : Section 68 of the Finance Act, 1994.

AUDIT CODE : ST-OSR99

The assessee are a provider of Banking and other financial Services. Income from assignment/Securitization of loans of Rs. 3805.10 lakhs has been reflected under scheduled 16 of their Balance Sheet for the year 2012-13. They sold banking products i.e. loans to different class of customers. The said loans were subsequently taken over by different Banks with the arrangement that the assessee would collect interest from the borrowers and would pay a portion of the interest accrued to the Banks as fixed by them from the borrowers and has been observed that remaining interest have been shown in their Balance Sheet as assignment/securitization of loan'. Further, they have shown separately, income of Interest Rs. 78229.50 lakhs as non-taxable in their Balance Sheet for the year 2012-13. Therefore, when they have sold the loans to the different bankers and the rights of the loan have also been transferred to the Banks. They are collecting interest from the borrowers on behalf of the Bank, it means they are acting as a commission agent. They are depositing a portion/percentage of interest to the Banks and the remaining interest portion lying with them should be treated as commission earned by them which have been reflected in their Balance Sheet for the year 2012-13 as income from assignment/securitization of loans valued Rs. 3805.10/- lakhs and is should be taxable under Business Auxiliary Service.

Therefore, they are liable to pay the Service Tax on the value of Rs. 3805.10 lakhs @ 12.36% amounting to Rs. 4,70,31,036/- under section 68 along with applicable interest under section 75 and Penalty under Section 73 of Finance Act, 1994.

OBJECTION NO. 6

GIST OF THE OBJECTION : Non Payment of Service Tax on R & D services Performed.

COMMISSIONERATE : Service Tax, Bangalore.

CONTRAVENTION OF PROVISION : Section 68 of the Finance Act, 1994.

AUDIT CODE : ST-OSR99

The assessee have two units registered as 100% EOUs. One of the unit is primarily engaged in the business of manufacturing and exporting solid dose pharmaceutical products and the other unit is primarily engaged in rendering Research and Development services. In the second unit, which is into provision of Research and Development services, the following services are performed and exported to their parent company.

1. Stability Studies
2. Technical Testing and Analysis of new drugs on Human Volunteers/participants.

Prior to 01.07.2012, the above two services performed and exported to the parent company and payment received in foreign convertible currency.

With effect from 01.07.2012, with introduction of Place of Provision of Services, 2012, services for which the goods are required to be made physically available to the provider of services when performed in taxable territory, do not qualify as export of service.

Accordingly, with effect from 01.07.2012, the assessee paid service tax on 'Stability Studies' of drug conducted in taxable territory, but however, had not paid service tax on 'technical testing and analysis of new drugs on Human Volunteers/Participant' claiming it as export of service as the consideration is received in foreign currency.

It may not be out of place to mention that technical testing and analysis of new drugs on Human Volunteers/Participants' i.e. clinical trials conducted by Clinical Research Organisation only is exempt from service tax by virtue of Notification No. 25/2012 ST dated 20.06.2012. It is pertinent to note that the assessee are not Clinical Research Organisations. On verification of the invoices raised by the assessee on parent company, it is observed that no service tax had been paid on such clinical trials conducted by them. The service tax liability on which works out to Rs. 10,46,66,545/- (Inclusive of cess).

The tax-payer did not agree to the Audit observation and contended that the services are exported and hence, does not attract service tax. They also contended that clinical trials are exempt from service tax.

The issue was deliberated during the AMC and decided and directed to issue SCN. SCN dated 27.08.2014 has been issued.