
STUDY MATERIAL

PROFESSIONAL PROGRAMME

ADVANCED TAX LAWS

AND PRACTICE

MODULE 3

PAPER 7



**THE INSTITUTE OF
Company Secretaries of India**

IN PURSUIT OF PROFESSIONAL EXCELLENCE

Statutory body under an Act of Parliament

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PROFESSIONAL PROGRAMME

ADVANCED TAX LAWS AND PRACTICE

This Study Material is designed for the benefit of the students preparing for the above subject under the Professional Programme and written in lucid and simple language for the benefit of the students.

The course material is unique in its treatment of various provisions of the relevant Acts. Income Tax, Central Excise, Customs, VAT and Service Tax pose the peculiar problem of being subjected to frequent changes either by legislative amendments or by issue of notifications, orders, trade notices etc. Every effort has been made to give the latest information, wherever possible including changes made by the Finance Act, 2013.

While writing the study material an attempt has been made to present the material in a unified and cohesive manner, giving the blend of provisions of Direct Tax Laws and Indirect Tax Laws. This paper comprises two parts. The first part (Part A) deals with 'Direct Tax Management' the second part (Part B) deals with the 'Central Excise, Customs, VAT and Service Tax'.

Company Secretaryship being a professional course, the examination standards are set very high, with emphasis on knowledge of concepts, applications, procedures and case laws, for which sole reliance on the contents of the study material may not be enough. Besides, Company Secretaries Regulations, 1982 requires the students to be conversant with the amendments to the laws made upto six months preceding the date of examination. This study material may therefore be regarded as basic material and must be read along with the Bare Act, Rules, Regulations, Case Law, leading journals and financial dailies in addition to various circulars and notifications, etc. issued from time to time by the CBDT and CBEC as well as suggested readings.

The various changes made upto 31st May, 2014 have been included in this study material. However, it may happen that some developments might have taken place during the printing of the study material and its supply to the students. The students are therefore advised to refer to the 'Student Company Secretary', 'Chartered Secretary' and other publications for updation of study material. In the event of any doubt, students may write to the Directorate of Academics and Perspective Planning in the Institute for clarification at academics@icsi.edu.

Although care has been taken in publishing this study material yet the possibility of errors, omissions and/or discrepancies cannot be ruled out. This publication is released with an understanding that the Institute shall not be responsible for any errors, omissions and/or discrepancies or any action taken in that behalf.

The students may note that Assessment Year for and December 2014 examinations is 2014-2015. Besides all other changes made through notification etc. and made effective six months prior to the examination will also be applicable. This study material is updated in accordance with the Finance Act, 2013 and is applicable for Assessment Year 2014-15 relevant for June 2014 and December 2014 examination.

The students should further note that the notified sections of the Companies Act, 2013 upto June 30, 2014 do not have any impact on Finance Act, 2013 which is applicable for December 2014 Examination (Assessment year 2014-15).

PROFESSIONAL PROGRAMME

SYLLABUS

FOR

PAPER 7: ADVANCED TAX LAWS AND PRACTICE (100 Marks)

Level of Knowledge: Advance Knowledge

Objective: To acquire Advance knowledge of the practical and procedural aspects of Direct and Indirect Tax Laws.

Detailed Contents:

PART A: Direct Tax Management (30 Marks)

Chapter 1: Taxation of Individual Entities, Partnership, LL.P, Companies.

Chapter 2: International Taxation Covering Taxation of Non Resident Entities, Advance Ruling, Transfer Pricing, Direct tax Avoidance Agreement.

Chapter 3: Case studies and Practical Problems covering Advance Tax Planning relating to Companies and Business Entities.

Part B: Central Excise, Customs, VAT and Service Tax (70 Marks)

1. Introduction

Special Features of Indirect Tax Levies - All Pervasive Nature, Contribution to Government Revenues; Constitutional Provisions Authorizing the Levy and Collection of Duties of Central Excise and Customs

2. Central Excise Laws

- Basis of Chargeability of Duties of Central Excise - Goods, Manufacture, Classification and Valuation of Excisable Goods
- CENVAT Credit Mechanism
- Registration, Assessment, Provisional Assessment, Manner of Payment of Duty, Exemption, Recovery and Refunds of Duties
- Clearance of Excisable Goods; Invoice System, Central Excise Bonds; Maintenance of Accounts and Records and Filing of Returns, Large Tax Payer Units, Excise Audit 2000, Audit u/s 14 and 14AA of Central Excise Act 1944
- Exemption to First Clearance of Specified Goods
- Export Incentives under Central Excise such as SEZs, STPI, EHTP, EPZ
- Investigation, Adjudication, Appeal and Revision, including Appearance before CESTAT by Company Secretary as Authorized Representative; Settlement of Cases, Advance Ruling
- Search, Seizure, Arrest, Prosecution and Compounding; Offences and Penalty
- Miscellaneous Provisions under Central Excise

3. Customs Laws

- Levy of Customs Duties, Types of Customs Duty Leviable, Tariff Classification & Exemptions, Valuation of Imported and Exported goods

- Provision of Assessment, Payment of Duties, Recovery and Refund of Customs Duties
- Duty Drawback
- Procedure for Clearance of Imported and Exported Goods
- Transportation and Warehousing
- Confiscation of Goods and Conveyances and Imposition of Penalties; Search, Seizure and Arrest, Offences and Prosecution Provisions
- Adjudication, Appeal and Revision; Settlement of Cases, Advance Ruling
- Other Relevant Areas and Case Studies under Custom Laws and Rules

4. **Promissory Estoppel in Fiscal Laws** – Principles and Applicability with reference to Indirect Taxes
5. **Tax Planning and Management** – Scope and Management in Customs, with Specific Reference to important Issues in the Respective Areas
6. Background, Negative List Approach, Statutory Provisions, Taxable Services, Valuation, Point of Taxation, Place of Provision of Service, Administrative Mechanism and Procedural Aspects, Assessment, Computation, Levy, Collection and Payment of Service Tax, Exemptions, CENVAT Credit for Service Tax, Returns, Refunds, Demands, Appeals, Revisions, Advance Rulings, Settlement Commission, Audit under Section 72A of Finance Act, 1994.
7. Goods and Service Tax (GST) – Concept and Developments
8. Background, Concept and Mechanism of VAT, Classification, Invoicing, Exemption, Returns, Refunds, Demands, Appeals, Revisions, Liability under VAT
9. Set off and Composition Scheme, Computation of VAT, Assessment, VAT on Works Contract, Right to use Property, Rate of Tax, Procedural Aspects including Registration, Preparation and Filing of E-Returns, Audit and Appearances

LIST OF RECOMMENDED BOOKS**MODULE 3****PAPER 7: ADVANCED TAX LAWS AND PRACTICE****Recommended Readings****I. Direct Taxes**

1. Girish Ahuja & Ravi Gupta : Professional Approach to Direct Taxes-Law and Practice; Bharat Law House (P) Ltd. 22, Tarun Enclave, Pitampura, New Delhi-110034.
2. E. A. Srinivas : Corporate Tax Planning; McGraw Hill Education (India) Ltd., B-4, Sector-63, Noida – 201 301.
3. Dr. V. K. Singhania : Direct Taxes Law and Practices; Taxmann Publications (P) Ltd; 59/32, New Rohtak Road, New Delhi – 110 005.
4. B.B. Lal and N. Vashist : Direct Taxes, Income Tax, Wealth Tax and Tax Planning; Darling Kindersley (India) Pvt. Ltd., 482, FIE, Patparganj, Delhi.- 110092

II. Indirect Taxes

1. V. S. Datey : Indirect Taxes – Law & Practices; Taxmann Publications, 59/32, New Rohtak Road, New Delhi-110 055.
2. Dr. Sanjeev Kumar : T-195, Mangolpuri Industrial Area, Phase-1, New Delhi-110083
3. V.S. Datey : Service Tax Ready Reckoner; Taxmann, Publications, 59/32, New Rohtak Road, New Delhi
4. J.K. Mittal : Law, Practice & Procedure of Service Tax; CCH India, [Walters Kluwer (India) Pvt. Ltd.], 501-A, Devika Tower, 6 Nehru Place, New Delhi.
5. Balram Sangal & Jagdish Rai Goel : All India VAT manual (4 Vols.); Commercial Law Publisheres (India) Pvt. Ltd., 151, Rajindra Market, Opp. Tis Hazari Courts, Delhi – 110 054

References:**I. Direct Taxes**

1. Bare Act : Income Tax Act & Rules and Wealth Tax Act & Rules
2. Annual Finance Act : <http://indiabudget.nic.in/index.asp>
3. Sampath Iyengars : Law of Income Tax, 11th Edition; Bharat Law House Pvt. Ltd., T-1/95, Mangolpuri Industrial Area, Phase I, New Delhi-110083.
4. Kanga & Palkhivala : Shalmadas Gandhi Marg, Chikal House , Opposite Bank of India, Princess Street,Mumbai
5. S. C. Mishra : Transfer Pricing Manual

II. Indirect taxes

1. R. K. Jain's : Central Excise and Custom Law Manual; Centax Publications Pvt. Ltd, 1512-B, Bhishm Pitamah Marg (Opp. ICICI Bank of Defence Colony), New Delhi-110003, India
2. Taxmann : CENVAT Law & Practice; Taxmann Allied Services (P) Ltd., 59/32, New Rohtak Road, New Delhi – 110005

Journals:

1. Chartered Secretary : ICSI, New Delhi
2. E-bulletin : Available at ICSI website www.icsi.edu
3. Income Tax Reports : Company Law Institute of India (P) Ltd., Chennai.
4. Taxmann : Taxmann Publications (P) Ltd., Chennai.
5. Tax and Corporate : Referencer, Bharat Law House (P) Ltd., 22, Tarun Enclave, Pitampura, New Delhi – 110 034.
6. Excise and Customs Cases : Fortnightly Reporting Journals; Indirect Tax Laws of India (P) Ltd., Chennai.
7. Excise Law Times : Fortnightly Reporting Journal; Centax Publications (P) Ltd. 1512-B, Sachdeva P.T. College of Defence Colony, New Delhi – 110 003



ARRANGEMENT OF STUDY LESSONS

PAPER 7: ADVANCED TAX LAWS AND PRACTICE (100 Marks)

<i>Lesson No.</i>	<i>Topic</i>
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PART A: DIRECT TAX MANAGEMENT

- I. Taxation of Individual, Partnership, LLP and Companies
- II. International Taxation
- III. Tax Planning and Tax Management

PART B: CENTRAL EXCISE, CUSTOMS, VAT AND SERVICE TAX

- IV. Indirect Tax Law and Practice: An Introduction
- V. Central Excise Law
- VI. Customs Laws
- VII. Advance Ruling, Settlement Commission and Appellate Procedure
- VIII. Promissory Estoppel in Fiscal Laws and Tax Planning
- IX. Service Tax: Introduction and Administration
- X. Procedural Aspects and Adjudication under Service Tax
- XI. Goods and Service Tax- Concept and Developments
- XII. Value Added Tax: Introduction and Procedural Aspects

TEST PAPERS

PROFESSIONAL PROGRAMME
ADVANCED TAX LAWS AND PRACTICE

CONTENTS

Lesson 1

LLP COMPANIES

Page

Lesson Outline	...	1
Learning Objectives	...	1
Introduction and Constitutional Provisions	...	2
What is Finance Act?	...	4

Part I: Basic Concepts and Taxation of Individuals

Basic Concepts	...	6
Computation of Taxable Income and Tax Liability of an Assessee	...	7
Tax Rates for AY 2014-15	...	9
Determination of Residential Status [Section 6]	...	11
Scope of Total Income [Section 5]	...	18
Various Heads of Income	...	21
Income under the Head Salaries (Section 15 to 17)	...	22
Income from House Property (Section 22 to 27)	...	35
Profits and Gains of Business or Profession (Section 28 to 44DB)	...	42
Capital Gains	...	63
Income from other Sources	...	67
Clubbing of Income	...	70
Set off and Carry Forward of Losses	...	71
Deductions from Gross Total Income u/s 80C to 80U	...	74
Self Test Questions	...	88

Part II: Taxation of Partnership Firms/Limited Liability Partnership

Assessment as a Firm [Section 184]	...	91
Taxation of Limited Liability Partnership (LLP)	...	94
Self Test Questions	...	101

Part III: Taxation of Companies

Constitutional Provisions	...	103
Meaning of Company	...	103
Categories of Companies	...	104
Tax Incidence on Company	...	106
Rates of Income Tax for the Assessment Year 2014-15	...	106
Minimum Alternate Tax (MAT)	...	107

Dividend Distribution Tax (DDT) (Section 115O)	...	111
Taxation of Foreign Dividends (Section 115BBD)	...	113
Self Test Questions	...	113

Lesson 2

INTERNATION TAXATION

PART I:TAXATION OF NON-RESIDENTS ENTITIES

Lesson Outline	...	115
Learning Objectives	...	115
Who is a Non-Resident?	...	116
Tax Incidence on Non Resident (Section 5)	...	117
Incomes Exempt in the hands of Non-Resident/Foreign company [Section 10]	...	120
Special provisions for computing profits and gains in case of Non-Residents [Deemed/Presumptive Income/Taxation]	...	121
Charge of Tax on Incomes Arising to Non Residents or Foreign Companies – Special Rates [Section 115A to 115BBA]	...	125
Special Provisions Relating to Certain Incomes of Non-Resident Indian Specified Asset (ii)	...	129
Self-Test Questions	...	131

PART II: ADVANCE RULING

Concept of Advance Ruling	...	132
Who can seek Advance Ruling?	...	132
Authority for Advance Ruling (AAR) (Section 245O)	...	133
Application for Advance Ruling (Section 245Q)	...	134
Powers of the Authority (Section 245U)	...	135
Applicability of Advance Ruling (Section 245S)	...	136
Question Precluded	...	136
Advance Ruling to be Void [Section 245T]	...	136
Self-Test Questions	...	137

PART III: TRANSFER PRICING

Introduction	...	138
Importance of transfer pricing	...	138
Transfer pricing provisions in india	...	139
What is arm's length price?	...	139
Associated Enterprises (AE)	...	140
Meaning of international transaction	...	141
Transfer pricing – Applicability to Domestic Transactions	...	143
Transfer Pricing – Methods	...	145
Reference to Transfer Pricing Officer	...	152
Advance Pricing Agreement	...	154
Transfer pricing – Documentation	...	157
Transfer Pricing – Penalty for Contravention	...	159
Self-Test Questions	...	160

PART IV: DOUBLE TAXATION AVOIDANCE AGREEMENTS

Agreements with Foreign Countries or Specified Territories (Section 90)	...	161
Adoption by Central Government of Agreement between Specified		
Associations for Double Taxation Relief (Section 90A)	...	162
Countries with which no Agreement Exists (Section 91)	...	162
Necessity for DTAA	...	164
Taxation of Income from Air and Shipping Transport under DTAA	...	165
Permanent Establishment (PE)	...	165
Foreign Tax Credit	...	166
Passive Foreign Investment Company (PFIC)	...	167
Self-Test Questions	...	168

Lesson 3**TAX PLANNING AND TAX MANAGEMENT**

Lesson Outline	...	169
Learning Objectives	...	169
Concept of Tax Planning	...	170
Tax Planning, Tax Avoidance and Tax Evasion	...	171
Difference between tax Planning, Tax Avoidance and Tax Evasion	...	172
Objectives of Tax Planning	...	173
Importance of Tax Planning	...	174
Essentials of Tax Planning	...	176
Types of Tax Planning	...	176
Tax Management	...	177
Areas of Tax Planning in the context of the Income-Tax Act, 1961	...	177
Form of the Organisation	...	177
Locational Aspects	...	182
Nature of Business	...	183
Some General Considerations Regarding New Business	...	184
Setting up and Commencement of Business vis-à-vis Tax Planning	...	185
Measures of Tax Planning in Relation to Setting Up and Commencement	...	186
Tax Planning Relating to Corporate Restructuring	...	187
Concept of Reverse Merger	...	188
Tax Planning Relating to Financial Management Decisions	...	189
Tax Planning Relating to Non-Residents	...	192
Tax Planning for Indian Collaborators	...	193
Tax Planning for Employees	...	194
Tax Planning under Wealth Tax Act	...	197
Planning in the Context of Court Rulings and Legislative Amendments	...	197
Statutory Force of the Notifications	...	198
Organisation of Tax Planning Cells	...	199
Lesson Round Up	...	200
Self Test Questions	...	200

Lesson 4**INDIRECT TAX LAWS AND PRACTICE -AN INTRODUCTION**

Lesson Outline	...	203
Learning Objectives	...	203
Introduction	...	204
Constitutional Provisions in Relation to Taxation	...	204
Indirect Taxes	...	205
Lesson Round Up	...	212
Self-Test Questions	...	213

Lesson 5**CENTRAL EXCISE LAW**

Lesson Outline	...	215
Learning Objectives	...	215

PART I: BASIS OF CHARGEABILITY OF EXCISABLE GOODS

Basis of Levy of Excise Duties	...	216
Chargeability of Excise Duty	...	216
Taxable Event	...	217
The concept of "Goods"	...	217
The concept of 'Excisable Goods'	...	223
Concept of Manufacture	...	224
Concept of "Manufacturer"	...	231
Self-Test Questions	...	232

PART II: CLASSIFICATION OF GOODS

Introduction	...	235
Purpose of Classification	...	235
Classification – salient features	...	235
Emergency Power of Central Government to Increase Duty	...	236
Rules for Interpretation (Common for Excise and Customs)	...	237
Cases Laws under Classification	...	240
Self-Test Questions	...	241

PART III: VALUATION OF EXCISABLE GOODS

Introduction	...	243
Rates of Duty	...	243
Methods of valuation	...	244
(1) Tariff values	...	244
(2) Valuation based on MRP [retail sale price] (Section 4A)	...	245
(3) Valuation based on Transaction Value (section 4)	...	249
Annexure: The Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000	...	261
Holding Company and Subsidiary Company	...	263
Self-Test Questions	...	266

**PART IV: REGISTRATION, ASSESSMENT, PAYMENT
CLEARANCE AND EXEMPTION OF DUTIES**

Introduction	...	269
Registration	...	270
Assessment	...	275
Payment of Excise Duties	...	278
Compounded Levy Scheme (Rule 15): Special Procedure for Payment of Duty	...	285
Excise Duty — Exemptions	...	290
Power to Grant Exemption from Duty of Excise (Section 5A)	...	291
Self-Test Questions	...	292

PART V: CENVAT CREDIT RULES, 2004

Introduction	...	295
Concept of CENVAT Credit	...	296
CENVAT Credit Rules, 2004	...	297
Special Audit in Cases Where Credit of Duty Availed or Utilized is not within the Normal Limits, etc. (section 14AA)	...	319
Case Studies	...	320
Self-Test Questions	...	322

PART VI: EXPORT BENEFITS AND PROCEDURES

Introduction	...	323
Types of Exporters	...	324
Excise Concessions for Exports	...	324
Export Procedures	...	324
Rebate of duty (Rule 18 of Central Excise Rules, 2002)	...	325
Export without payment of duty under bond (rule 19 of Central Excise Rules, 2002)	...	333
Other Miscellaneous Provisions	...	339
Various Bonds under Excise	...	340
Self - Test Questions	...	340

PART VII: RECOVERY AND REFUNDS OF DUTIES UNDER CENTRAL EXCISE

Introduction	...	342
Refunds	...	342
Refund of Duty (Section 11B)	...	343
Doctrine of Unjust Enrichment	...	344
Consumer Welfare fund: (Section 12C)	...	345
Interest on Delayed Refunds (Section 11BB)	...	345
Demands of Duty [Section 11A]	...	346
Interest on Delayed Payment of Duty (Section 11AA)	...	350
Mode of Recovery (Section 11)	...	350
Penalty in Certain Cases [Section 11AC]	...	351
Power not to Recover Duty of Excise not Levied or Short Levied as General Practice (Section 11c)	...	351

	<i>Page</i>
Duties Collected from Buyer to be Deposited with the Government [Sections 11D and 11DD]	352
Excise Audit—2000	353
Special Audit in Certain Cases (Section 14A)	354
Quick Reference Table	355
Self-Test Questions	356

PART VIII: SMALL SCALE UNITS - APPLICABLE LAWS FOR EXCISE DUTY CONCESSIONS

Introduction	357
Salient Features and Coverage of Exemption Notifications	357
General Exemption Scheme under Notification No. 8/2003-C.E.	357
SSIS – Notification 8/2003-CE	358
Conditions for Claiming the Exemptions Based on Clearances	362
Benefits to SSIS	362
CENVAT Credit Implications and Applicable Provisions	363
Self-Test Questions	365

PART IX: OFFENCES, SEARCH & SEIZURE AND ADJUDICATION PROCEDURES

Offences and Penalties (Section 9)	368
Search and Siezure	370
Rules for Search and Seizure	372
Powers of Adjudication	374
Self-Test Questions	375

Lesson 6

CUSTOMS LAW

Lesson Outline	376
Learning Objectives	376

PART I: INTRODUCTION AND BASIC CONCEPTS OF CUSTOMS LAW

Introduction	377
Statutory Provisions of Customs Act, 1962	377
Limbs of Customs Law	379
Levy of Custom Duty	381
Taxable Event	381
Types of Duties under Customs	381
Important Definitions	389
Self-Test Questions	392

PART II: VALUATION, ASSESSMENT OF IMPORTED AND EXPORT GOODS AND PROCEDURAL ASPECTS

Introduction	...	393
Valuation of Goods For Levy of Customs Duty	...	394
Valuation of Imported Goods	...	394
Valuation of Export Goods	...	407
Assessment of Duty	...	411
Provisional Assessment of Duty [Section 18]	...	412
Determination of Duty Where Goods Consist of Articles Liable to Different Rates of Duty (Section 19)	...	413
Re-Importation of Goods (Section 20)	...	413
Duty on Pilfered Goods (Section 13)	...	414
Goods Derelict, Wreck, Etc. (Section 21)	...	414
Abatement of Duty on Damaged or Deteriorated Goods (Section 22)	...	414
Remission of Duty on Lost, Destroyed or Abandoned Goods (Section 23)	...	415
Denaturing or Mutilation of Goods (Section 24)	...	415
Power to Grant Exemption from Duty (Section 25)	...	416
Refund and Recovery Provisions (Section 26 To 28D)	...	418
Self Test Question	...	426

PART III: ARRIVAL OR DEPARTURE AND CLEARANCE OF IMPORTED OR EXPORT GOODS

Introduction	...	429
Provisions Relating to Conveyances Carrying Imported or Export Goods	...	429
Provisions Relating To Arrival or Departure Of Goods	...	431
Clearances of Imported Goods And Export Goods (Section 44 To 51)	...	435
Clearance of Export Goods	...	440
Procedure for Exports through Inland Container Depots	...	445
Goods in Transit (Section 52 to 56)	...	448
Self Test Question	...	452

PART IV: WAREHOUSING, DUTY DRAWBACK, BAGGAGE AND MISCELLANEOUS PROVISIONS

Warehousing (Section 57 to 73)	...	453
Case Studies	...	464
Duty Drawback (Section 74 to 76)	...	465
Baggage (Section 77 to 81)	...	473
Goods Imported Or Exported By Post [Section 82 to 84]	...	479
Stores [Section 85 to 90]	...	479
Provisions Relating to Coastal Goods and Vessels Carrying Coastal Goods [Section 91 to 99]	...	481
Self Test Questions	...	483

PART V: SEARCH, SEIZURE, CONFISCATION OF GOODS, OFFENCES AND PENALTIES

Searches, Seizure and Arrest	...	485
Confiscation of Goods (Section 111 To 127)	...	490
Offences and Prosecution Provisions (Section 132 to 140A)	...	499
Self Test Questions	...	505

Lesson 7**ADVANCE RULING, SETTLEMENT COMMISSION AND APPELLATE PROCEDURE**

Lesson Outline	...	507
Learning Objectives	...	507
Advance Ruling	...	508
Settlement Commission	...	512
Appellate Procedures	...	516
Appellate Scheme under Central Excise	...	517
Monetary Limits for Filing of Appeal	...	517
Appeals before Commissioner (Appeals) [Section 35]	...	518
Customs, Excise and Service Tax Appellate Tribunal	...	519
Further Remedies after Decision by CESTAT	...	523
Powers Of Committee Of Chief Commissioners of Central Excise or Commissioner of Central Excise to Pass Certain Orders on its Own (Section 35E)	...	524
Deposit, Pending Appeal, of Duty Demanded or Penalty Levied (Section 35f)	...	525
Interest on Delayed Refund of Amount Deposited under the Proviso to Section 35f (Section 35ff)	...	525
Revisionary Role of the Central Government [Section 35EE]	...	525
Adjudication and Appellate Provisions under Customs Laws	...	526
(A) Appeals to Commissioner (Appeals)(Section 128)	...	527
(B) Appellate Tribunal (Section 129)	...	527
Lesson Round Up	...	536
Self Test Questions	...	536

Lesson 8**PROMISSORY ESTOPPEL IN FISCAL LAWS, TAX PLANNING AND TAX MANAGEMENT**

Lesson Outline	...	539
Learning Objectives	...	539
Meaning of Doctrine of Promissory Estoppel	...	540
Requirements of Promissory Estoppel	...	540
Doctrine of Promissory Estoppel And Fiscal Laws	...	541
Case Studies	...	543
Limitation of the Doctrine	...	544
Tax Planning	...	544
Customs Act and Tax Planning	...	545
Excise Law and Tax Planning	...	551
Lesson Round Up	...	555
Self-Test Questions	...	556

Lesson 9**SERVICE TAX: INTRODUCTION AND ADMINISTRATION**

Lesson Outline	...	557
Learning Objectives	...	557

	<i>Page</i>
Background	558
Constitutional Validity	559
Administrative Mechanism	560
Taxability of Services	561
Limbs of Service Tax Laws	561
Meaning of Service	563
(A) Declared Services	564
(B) Negative List of Services	565
(C) List of Exemptions Under Mega Notification	567
(D) Place of Provision of Services Rules	580
Rate of Service Tax	584
Rounding Off of Service Tax	584
Lesson Round Up	585
Self Test Questions	585

Lesson 10

PROCEDURAL ASPECTS AND ADJUDICATION UNDER SERVICE TAX

Lesson Outline	587
Learning Objectives	587
Registration	588
Service Tax Registration of Special Category of Persons	589
Payment of Service Tax	589
Incidence to Pay Service Tax	591
Due Date for Payment of Service Tax	594
Adjustment of Service Tax	595
Valuation of Taxable Services	595
Abatement in Service Tax	597
Records to be Maintained	597
Returns under Service Tax	597
Penalty for Not Filing and late Filing of Return	598
Penalties and Prosecution	598
Waiver or Reduction of Penalty	600
Prosecution	600
CENVAT Credit Rules, 2004	600
Advance Ruling (Section 96a To 96-I)	601
Application for Advance Ruling	601
Appeals	602
Appeal to Tribunal (Section 86)	603
Settlement Commission	603
Special Audit under Section 72a	605
Role of Company Secretaries	605
Lesson Round Up	606
Self Test Questions	607

Lesson 11	
GOODS AND SERVICE TAX- CONCEPT AND DEVELOPMENTS	
Lesson Outline	...
Learning Objectives	...
Introduction	...
What Is Goods And Service Tax	...
Justification of GST	...
Salient Features Of The GST Model	...
Central and State Taxes to be Subsumed under GST	...
Rate Structure under GST	...
Highlights of the Constitution (One Hundred And Fifteenth Amendment) Bill, 2011	...
Lesson Round Up	...
Self Test Questions	...

Lesson 12	
VALUE ADDED TAX: INTRODUCTION AND PROCEDURAL ASPECTS	
Lesson Outline	...
Learning Objectives	...
Historical Background	...
Concept of Vat	...
Registration	...
Invoice	...
Composition and Set off Scheme	...
Returns	...
Rates of Tax	...
Credit and Set-off Under Vat	...
Exempted Sale	...
Samples or Gifts	...
Consignment Transfer	...
Zero Rating	...
Work Contract Tax	...
Computation and Methods of Vat	...
Assessment	...
Vat Audit	...
Refunds	...
Scrutiny Process	...
Appeals, Revision and Appearances	...
Role and Position of Company Secretaries	...
Lesson Round Up	...
Self Test Questions	...

TEST PAPERS	
Test Paper 1	...
Test Paper 2	...

Lesson 1

Taxation of Individuals, Partnership Firms/ LLP and Companies

LESSON OUTLINE

This lesson is divided into three parts;

- I. BASIC CONCEPTS AND TAXATION OF INDIVIDUALS
- II. TAXATION OF FIRM/LIMITED LIABILITY PARTNERSHIP (LLP)
- III. TAXATION OF COMPANIES

LEARNING OBJECTIVES

Income tax is a direct tax levied on the income earned by Individuals, Partnership firms, Limited Liability Partnerships, Corporations or by other forms of business entities. The Indian constitution has empowered only the Central Government to levy and collect income tax. For all the matters relating to Income tax, the Income-Tax Act, 1961 is the umbrella Act which empowers the Central Board of Direct Taxes to formulate rules (The Income Tax Rules, 1962) for implementing the provisions of the Act.

After completing this lesson, students will have the understanding of:

- Basic concepts of taxation
- Constitutional provisions
- Definitions, Concept of Previous and Assessment year
- Residential Status and Scope of Total Income.
- Computation of Income Tax under five heads of Income: Salary, Income from House Property, Profit and Gains from Business or Profession, Capital Gains and Income from other sources.
- Deductions available under Chapter VI-A
- Determination of Total Income and Tax Liability of various entities like Partnership Firm, LLP Companies etc.

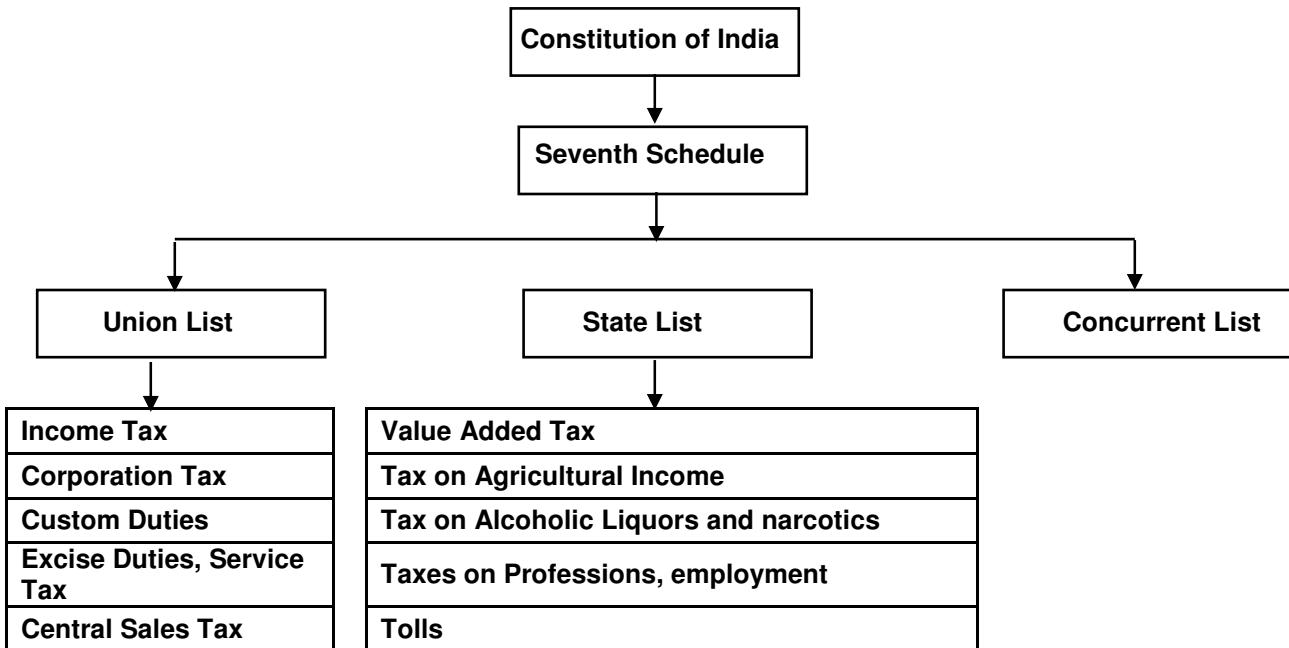
The Income Tax department is governed by the Central Board for Direct Taxes (CBDT). The CBDT is a part of Department of Revenue in the Ministry of Finance. It has been charged with all the matters relating to direct taxes in India. It provides essential inputs for policy and planning of direct taxes in India and is also responsible for administration of direct tax laws through the Income Tax Department.

INTRODUCTION AND CONSTITUTIONAL PROVISIONS

India is a federal union of States with distribution of powers. Articles 245 to 255 of the Constitution of India relate to legislative relations between the Union and States in the form of distribution of legislative powers between the Parliament and the Legislature of a State.

Powers to make laws are conferred by Articles 245, 246 and 248 of the Constitution while subject matters of laws to be made by Parliament and Legislature of a State are listed in Schedule VII to the Constitution.

Distribution of legislative powers is stipulated in **Article 246 read with Schedule VII of the Constitution** of India. There are three lists in Schedule VII in respect of which Union or State or both will have concurrent powers to make laws.



In respect of subject matters in the List I of Seventh Schedule i.e. Union List, Union shall have the exclusive power of making laws. In respect of subject matters in the List II of Seventh Schedule i.e. State List, State legislature shall have the exclusive power of making laws. Whereas in respect of subject matters in the List III i.e. Concurrent List, Parliament and States have concurrent powers to make laws.

In respect of levy of taxes and duties, Union and States have respective powers under Union List and State List, the summary of which is provided as under:

Union List

Amongst others, power to levy following taxes and duties are provided in the Union List:

1. Taxes on Income other than agricultural income;
2. Corporation tax;
3. Custom duties;
4. Excise duties except on alcoholic liquors and narcotics;
5. Estate and succession duties other than on agricultural land;

6. Taxes on the capital value of the assets; except agricultural land of individual and companies;
7. Rates of stamp duties on financial documents;
8. Taxes other than stamp duties on transactions in stock exchanges and future markets;
9. Taxes on sale or purchase of newspapers and on advertisements published therein;
10. Taxes on railway freight and fares;
11. Terminal taxes on goods or passengers carried by railways, sea or air; and
12. Taxes on the sale or purchase of goods in the course of Inter-State trade.
13. Taxes on services.

Entry No. 97 of List I of Seventh Schedule to the Constitution of India describes the residual powers of Parliament to make laws.

State List

Amongst others, power to levy following taxes and duties are provided in the State List:

1. Land Revenue;
2. Taxes on the sale and purchase of goods except newspapers;
3. Taxes on agricultural income;
4. Taxes on land and buildings;
5. Succession and estate duties on agricultural land;
6. Excise on alcoholic liquors and narcotics;
7. Taxes on the entry of goods into a local area;
8. Taxes on mineral rights, subject to any limitations imposed by Parliament;
9. Taxes on consumption and sale of electricity;
10. Taxes on vehicles, animals and boats;
11. Stamp duties except those on financial documents;
12. Taxes on goods and passengers carried by road or inland water ways;
13. Taxes on luxuries including entertainment, betting and gambling;
14. Tolls;
15. Taxes on professions, trades, callings and employment;
16. Capitation taxes; and
17. Taxes on advertisement other than those contained in newspapers.

Article 265 of the Constitution provides that no tax shall be levied or collected except by authority of law. Thus, the tax proposed to be levied or collected must be within the legislative competence of the legislature imposing the tax. The law imposing the tax, like other laws, must not violate any fundamental right.

Article 268 to 281 relate to the distribution of revenues between the Union and States. Stamp duties like those on financial documents and excise on medicinal or toilet preparations as mentioned in the Union list are to be levied by the Government of India but are to be collected by the States. Taxes on Inter-state trade or commerce by way of sale or purchase of goods and taxes on the consignment of goods are to be levied and collected by the Government of India but are to be assigned to the States (Article 269). All taxes and

duties referred to in the Union list except those referred to in Articles 268 and 269, surcharge on taxes and duties and any cess levied by the Parliament for specific purposes are to be collected by the Government of India and are to be distributed between the Union and the States in the manner prescribed by the President by order. Prior recommendation of the President of India is required to Bills affecting taxation in which States are interested under Article 274 of the Constitution of India.

Income tax being direct tax happens to be the major source of revenue for the Central Government. The entire amount of income tax collected by the Central Government is classified under the head:

1. Corporation Tax (Tax on the income of the companies); and
2. Income tax (Tax on income of the non-corporate assessee)

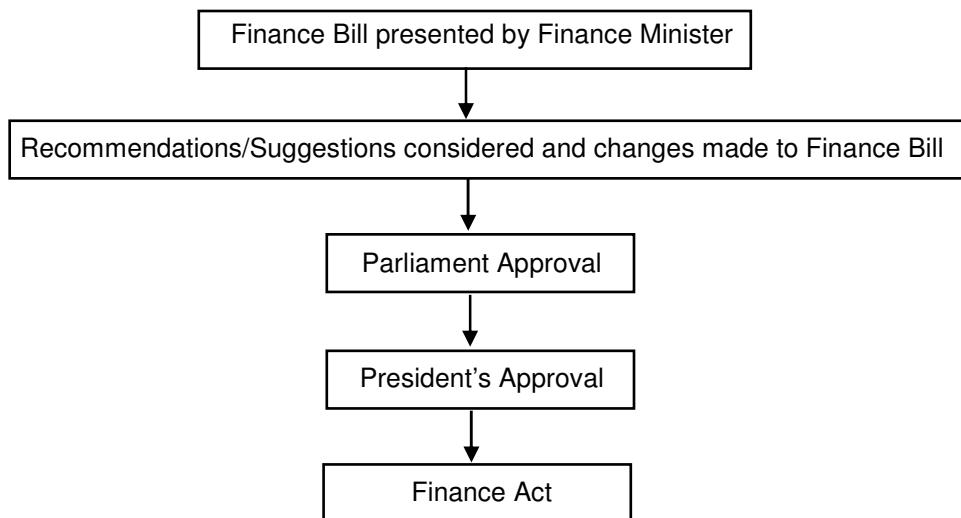
The classification of Income tax into above two categories is of great assistance to Central Government while preparing budget estimates and setting the target. **It is also important for easy division of tax between the Central and State Government as the proceeds from Corporation tax are not divisible with the States [Article 270(1) read with Article (4)(a)].**

WHAT IS FINANCE ACT?

The Finance Act contains necessary amendments in the Direct taxes (e.g. Income tax and Wealth tax) and Indirect taxes (e.g. Excise duties, custom duties and Service tax) signifying the policy decisions of the Union Government.

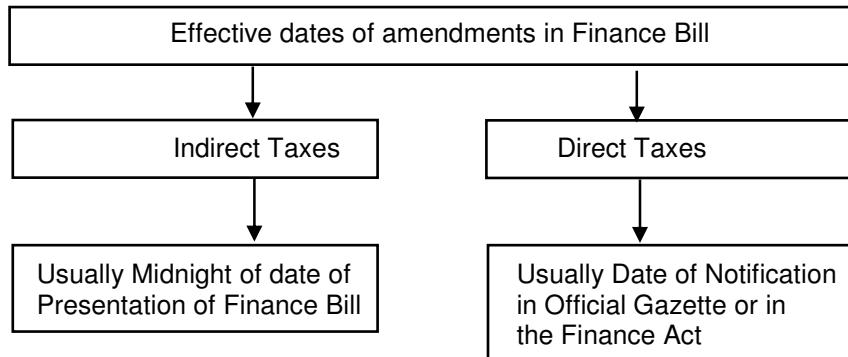
Finance Bill is presented usually in the last week of February every year and this bill contains amendments in direct as well as indirect taxes. It is usually presented in the Parliament by the Finance Minister.

The finance bill is passed by both the houses of Parliament after it is being tabled and necessary recommendation/amendments have been made in it. Once this bill has been passed by the Parliament, it goes to the President for his assent. After President's assent, the finance bill becomes the Finance Act.



The effective date of applicability of provisions of the Finance Act is usually mentioned in the notification in the official gazette or in the Act itself. Generally, the amendments by the Finance Act are made applicable from the first day of the next financial year e.g. generally, amendments by Finance Act, 2013 are effective

from 1st April, 2014. Regarding indirect taxes, the *ad valorem* tax rates (tax rates based on value) are effective from the midnight of the date of presentation of the Union Budget.



The First schedule to the annual Finance Act is divided into four parts:

Part I provides rates for current Assessment Year. For example, Part I of the Finance Act, 2013 provides income-tax rates for Assessment Year 2013-14;

Part II provides rates of TDS for the current financial year. For example, Part II of the Finance Act, 2013 provides rates of TDS for financial year 2013-14 (i.e. Assessment Year 2014-15);

Part III provides the rate of TDS under the head Income from 'Salaries' and the rates of advance tax for the current financial year. For example, Part III of the Finance Act, 2013 provides rates of advance tax for financial year 2013-14 (i.e. Assessment Year 2014-15).

Part IV provides for rules for computation of net agricultural income.

TAXATION OF INDIVIDUALS, PARTNERSHIP FIRMS/LLP AND COMPANIES

PART I: BASIC CONCEPTS AND TAXATION OF INDIVIDUALS

After completion of this part, a student will:

- Understand basic concepts of taxation: such as, definitions, concept of previous year and assessment year, Residential Status and Scope of Total Income;
- Able to compute Tax liability of individuals;
- Be familiar with tax provisions such as computation of total income, deduction under Section VI-A etc. pertaining to individuals.

Under the Income-Tax Act, 1961, total income of the previous year of every person, shall be charged to income tax in the assessment year at the rates laid down by the Finance Act for that assessment year. In other words, the income earned in a year is taxable in the next year and the income-tax rates prescribed for an assessment Year are applicable in respect of income earned during the previous Year.

BASIC CONCEPTS

Assessment Year and Previous Year

As per Section 2(9) of the Act, "Assessment Year" means the period of twelve months commencing on the 1st day of April every year.

As per Section 3 of the Act, the financial year in which the income is earned is known as the previous year. The financial year following a previous year is known as the assessment year. The assessment year is the year in which the income earned in the previous year is taxable. Any financial year begins from 1st of April of every year and ends on 31st of March of the subsequent year.

In case of a business or profession which is newly started, the previous year commences from the date of commencement of the new business or profession up to the next 31st March, unless the person is an existing assessee for any source of income.

General Rule: Income earned during a previous year is taxable in the Assessment Year.

Exceptions to General Rule:

Income earned during a previous year is taxable in the previous year itself in following cases:

- Income of Non-resident shipping companies [Sec 172]
- Income of persons leaving India with no intention of returning to India [Sec 174]
- Assessment of Association of Persons (AOP)/Body of Individuals (BOI) /Artificial Juridical Person (AJP) formed for a particular purpose likely to be dissolved in the same year of formation [Sec 174A]
- Transfer of assets with a view to avoid tax [Sec 175]
- Income of a discontinued business [Sec 176]

Person [Section 2(31)]: It includes Individual, HUF, Firm (or Limited Liability Partnership), Company, AOP/BOI – whether incorporated or not, Local Authority, AJP (Artificial Juridical Person).

Assessee [Section 2(7)]: It means person by whom any sum of tax, interest or penalty is payable. It includes a person in respect of whom any proceeding has been undertaken, a deemed assessee and an assessee in default.

COMPUTATION OF TAXABLE INCOME AND TAX LIABILITY OF AN ASSESSEE

Income tax is a charge on the assessee's income. Income Tax law lays down the provisions for computing the taxable income on which tax is to be charged. Taxable income of an assessee and tax liability shall be calculated in the following manner:

1. Determine the residential status of the person as per section 6 of the Act.
2. Calculate the income as per the provisions of respective heads of income. Section 14 classifies the income under five heads:
 - (i) Income from salaries
 - (ii) Income from House Property
 - (iii) Profits and gains of business or Profession
 - (iv) Capital Gains
 - (v) Income from other sources
3. Consider all the deductions and allowances given under the respective heads before arriving at the net income.
4. Exclude the income exempt under section 10 of the Act.
5. Aggregate of incomes computed under the 5 heads of income after applying clubbing provisions and making adjustments of set off and carry forward of losses is known as Gross Total Income.
6. Deduct there from the deductions admissible under Sections 80C to 80U. The balance is called Total income. The total income is rounded off to the nearest multiple of Rupees ten (Section 288A).
7. Add agriculture income in the total income calculated in (6) above. Then calculate tax on the aggregate as if such aggregate income is the Total Income.
8. Calculate income tax on the net agricultural income as increased by ₹ 2,00,000/2,50,000/5,00,000 as the case may be, as if such increased net agricultural income were the total income.
9. The amount of income tax determined under (8) above will be deducted from the amount of income tax determined under (7) above.
10. Calculate income tax on capital gains under Section 112, and on other income at specified rates.
11. The balance of amount of income tax left as per (9) above plus the amount of income tax at (10) above will be the income tax in respect of the total income. Applicable surcharge, if any would be levied. Marginal relief would be provided in cases where the assessee's income marginally exceeds the total income on the basis of which surcharge is leviable and the increase in total tax is more than increase in total income. Education Cess @ 2% and Secondary and Higher education cess @ 1% will be applied on tax including surcharge.
12. Deduct the following from the amount of tax calculated under (11) above:
 - Tax deducted and collected at source.
 - Advance tax paid.
 - Self Assessment tax
 - Double taxation relief.
13. The balance of amount left after deduction of items given in (12) above, shall be the net tax payable or net tax refundable for the assessee. Net tax payable/refundable shall be rounded off to the nearest multiple of Ten rupees (Section 288B).

14. Along with the amount of net tax payable, the assessee shall have to pay penalties or fines, if any, imposed on him under the Income-tax Act.

The steps involved for calculation of Taxable Income are discussed in brief as follows:

Particulars	Amount (₹)
Income (taxable) under the head:	
Income from Salaries	
+ Income from House Property	XXX
+ Profits and gains of business or profession	XXX
+ Capital gains	XXX
+ Income from other sources	XXX
	<u>XXX</u>
Adjustment in respect of:	
+ Clubbing of Income	XXX
– Set off and carry forward of losses	(XXX)
	<u>XXX</u>
= Gross Total Income	XXX
– Deductions under section 80C to 80U (or Chapter VIA)	<u>(XXX)</u>
= Total (Taxable) Income	<u>XXX</u>

The steps involved for calculation of tax liability are discussed in brief as follows:

Particulars	Amount (₹)
Tax on Special Incomes @ specified tax rates (Long term capital gains @ 20%; Casual Income @ 30% and Short term capital gains (on Securities transaction tax paid securities) @ 15%;	
Add: Tax on Balance Income @ Slab Rate/Flat Rate (as applicable)	XXX
Total Tax	<u>XXX</u>
Add: Surcharge, if any	XXX
Less: Marginal Relief, if applicable	<u>(XXX)</u>
Tax including Surcharge	XXX
Add: Education Cess @ 2% on tax including surcharge	XXX
Add: SHEC @ 1% on tax including surcharge	XXX
= Tax liability	<u>XXX</u>
Add: Interest under Section 234A/234B/ 234C	XXX
= Net tax liability	<u>XXX</u>
Less: Taxes paid by way of:	
– Tax deducted at source (TDS)	<u>(XXX)</u>
– Advance tax	<u>(XXX)</u>
– Self Assessment Tax	<u>(XXX)</u>
– Double Taxation Relief	<u>(XXX)</u>
Tax Payable (Refund)	<u>XXX</u>

TAX RATES FOR AY 2014-15

(A) Individual (other than in B or C below), Hindu undivided family, association of persons, body of individuals (other than Co-operative society), artificial juridical person:

Total Income (₹)	Tax Rate	Tax liability (₹)
Upto 2,00,000	Nil	Nil
2,00,001 – 5,00,000	10%	10% of (Total Income – 2,00,000)
5,00,001 – 10,00,000	20%	20% of (Total Income – 5,00,000) + 30,000
Above 10,00,000	30%	30% of (Total Income – 10,00,000) + 1,30,000

(B) Resident individual of the age of sixty years or more but less than eighty years at any time during the previous year

Total Income (₹)	Tax Rate	Tax liability (₹)
Upto 2,50,000	Nil	Nil
2,50,001 – 5,00,000	10%	10% of (Total Income – 2,50,000)
5,00,001 – 10,00,000	20%	20% of (Total Income – 5,00,000) + 25,000
Above 10,00,000	30%	30% of (Total Income – 10,00,000) + 1,25,000

(C) Resident Individual of the age of eighty years or more at anytime during the previous year

Total Income (₹)	Tax Rate	Tax liability (₹)
Upto 5,00,000	Nil	Nil
5,00,001 – 10,00,000	20%	20% of (Total Income – 5,00,000)
Above 10,00,000	30%	30% of (Total Income – 10,00,000) + 1,00,000

Rebate of income-tax in case of certain individuals [Section 87A introduced by Finance Act, 2013]

An assessee, being an individual resident in India, whose total income does not exceed five hundred thousand rupees, shall be entitled to a deduction, from the amount of income-tax on his total income with which he is chargeable for any assessment year, of an amount equal to hundred per cent of such income-tax or an amount of two thousand rupees, whichever is less.

The rebate shall be equal to the amount of income-tax payable on the total income for any assessment year or an amount of two thousand rupees, whichever is less. Consequently any individual having income up to ₹2,20,000 will not be required to pay any tax and every individual having total income above ₹ 2,20,000/- but not exceeding ₹5,00,000/- shall get a tax relief of ₹ 2000/-.

(D) Co-operative Society:

Total Income (₹)	Tax Rate	Tax liability (₹)
Upto 10,000	10%	10% of Total Income
10,001 – 20,000	20%	20% of (Total Income – 10,000) + 1,000
Above 20,000	30%	30% of (Total Income – 20,000) + 3,000

(E) Firms (including LLP):

Tax Rate on Total Income: 30%

(F) Local Authorities:

Tax Rate on Total Income: 30%

Common points in relation to (A) TO (F):

Surcharge: It will be levied at the rate of **ten per cent** of such income-tax in case of a person having a total income **exceeding one crore rupees**.

Marginal Relief: However, the total amount payable as income-tax and surcharge on total income exceeding one crore rupees shall not exceed the total amount payable as income-tax on a total income of one crore rupees by more than the amount of income that exceeds one crore rupees.

(G) Companies

Domestic Company:

Tax rate on Total Income: 30%

Company other than a domestic company:

Tax rate on total Income: 40%

Surcharge in case of Company

The amount of income-tax shall be increased by a surcharge for purposes of the Union calculated,-

- (i) in the case of every domestic company,-
 - (a) having a total income exceeding one crore rupees but not exceeding ten crore rupees, at the rate of five per cent of such income-tax; and
 - (b) having a total income exceeding ten crore rupees, at the rate of ten per cent of such income-tax;
- (ii) in the case of every company other than a domestic company,-
 - (a) having a total income exceeding one crore rupees but not exceeding ten crore rupees, at the rate of two per cent of such income-tax; and
 - (b) having a total income exceeding ten crore rupees, at the rate of five per cent of such income-tax:

Marginal Relief

However, in the case of every company having a total income exceeding one crore rupees but not exceeding ten crore rupees, the total amount payable as income-tax and surcharge on such income shall not exceed the total amount payable as income-tax on a total income of one crore rupees by more than the amount of income that exceeds one crore rupees:

Further in the case of every company having a total income exceeding ten crore rupees, the total amount payable as income-tax and surcharge on such income shall not exceed the total amount payable as income-tax and surcharge on a total income of ten crore rupees by more than the amount of income that exceeds ten crore rupees.

Note: In other cases (including sections 115-O, 115QA, 115R or 115TA) the surcharge shall be levied at the rate of ten per cent.

Education Cess and Secondary & Higher Education Cess

For financial year 2013-14, additional surcharge called the "Education Cess on income-tax" and "Secondary and Higher Education Cess on income-tax" shall continue to be levied at the rate of two per cent, and one per cent, respectively, on the amount of tax computed, inclusive of surcharge (wherever applicable), **in all cases**. No marginal relief shall be available in respect of such Cess.

DETERMINATION OF RESIDENTIAL STATUS [SECTION 6]

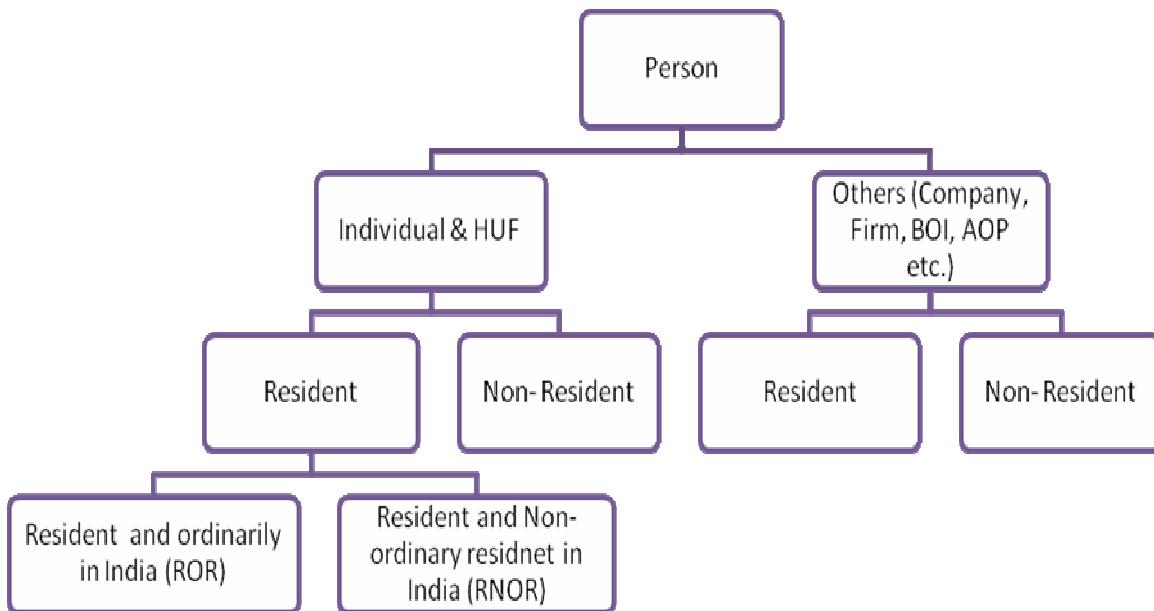
Total income of an assessee cannot be computed unless the person's residential status in India during the previous year is known. Section 6 of the Income-tax Act prescribes the tests to be applied to determine the residential status of all tax payers for the purposes of income-tax. According to the provisions relating to residential status, a person can either be;

- (i) Resident in India or
- (ii) Non-resident in India

However, individual and HUF cannot be simply called resident in India. If individual or HUF is a resident in India, they will be either;

- (a) Resident and ordinarily resident in India (ROR) or
- (b) Resident but not ordinarily resident in India (RNOR or NOR).

Persons other than individual and HUF will be either resident in India or non-resident in India.



1. Residential Status of Individual [Section 6(1) and 6(6)]

Provisions relating to determination of residential status of individuals are summarised as follows:

Resident If satisfies any one of the two basic conditions.

Non-Resident If does not satisfy any one of the two basic conditions.

Basic Conditions	<ol style="list-style-type: none"> Stay of Individual in India should be 182 days or more during relevant Previous Year (PY); OR Stay of Individual in India should be 60 days or more during relevant PY and 365 days or more during 4 PYs immediately preceding relevant PY.
Exception to Basic Conditions	<p><i>In following cases, only 1st Basic condition needs to be checked:</i></p> <ol style="list-style-type: none"> Indian Citizen <ul style="list-style-type: none"> - who comes on a visit to India during relevant PY; or - who is a crew member of an Indian Ship; or - who goes abroad for employment purposes. Person of Indian Origin (who himself or his parents or his grandparents were born in undivided India) who comes on a visit to India during relevant PY
ROR	If Resident Individual satisfies both the additional conditions.
RNOR	If Resident Individual does not satisfy both the additional conditions.
Additional Conditions	<ol style="list-style-type: none"> Individual should be resident (by satisfying any of the two basic conditions or first basic condition, if falls in exception to basic conditions) in at least 2 PYs out of 10 PYs immediately preceding relevant PY; and Stay of Individual in India should be 730 days or more during 7 PYs immediately preceding relevant PY.

Steps to be followed for determination of Residential status of a Person:

Step 1: Check whether an Individual falls under any exception to basic conditions.

Step 2: If yes, check only first basic condition, otherwise check both the basic conditions. If he satisfies any one of the basic conditions (only first in case of exception), then he would be resident in India, otherwise he would be Non-resident in India.

Step 3: If an Individual is resident in India, then check whether he is ROR or RNOR.

Step 4: If Individual satisfies both the additional conditions, then he is ROR. Otherwise, he would be RNOR.

Illustration

Determine the residential status of A for AY 2014-15

A is an Indian Citizen and goes from India to Spain for visit purposes on 27th December, 2013. Prior to this, he had never been out of India.

Solution

Determination of Residential status of A for Previous Year 2013-14 (Assessment Year 2014-15):

In this case, both the basic conditions would be checked as A does not fall under any exception to basic conditions.

Stay of A in India during relevant PY 2013-14 = 1st April, 2013 to 27th December, 2013 i.e. 271 days (30 + 31 + 30 + 31 + 31 + 30 + 27).

A is a Resident in India as he satisfies first basic condition by staying in India for more than 182 days during relevant previous year.

Now, it would be checked whether A is ROR or RNOR.

Since A had never been out of India before 27th December, 2013, he would be satisfying both the additional conditions as follows:

Additional Condition 1:

Resident in at least 2 PY out of 10 PYs:

PY	Falls under exception to basic condition	Stay during relevant PY (days)	First Basic Condition	Stay during 4 PY immediately preceding relevant PY	Second basic condition	Residential status
2012-13	No	365	Satisfied	Not required	Not required	Resident
2011-12	No	366	Satisfied	Not required	Not required	Resident

A satisfies 1st additional condition as he is resident in at least 2 PYs out of 10 PYs immediately preceding relevant previous year.

Additional condition 2:

Stay of Individual in India during 7 PY immediately preceding relevant PY:

PY	Stay Period	Days
2012-13	1 st April, 2012 to 31 st March, 2013	365
2011-12	1 st April, 2011 to 31 st March, 2012	366
2010-11	1 st April, 2010 to 31 st March, 2011	365
2009-10	1 st April, 2009 to 31 st March, 2010	365
2008-09	1 st April, 2008 to 31 st March, 2009	365
2007-08	1 st April, 2007 to 31 st March, 2008	366
2006-07	1 st April, 2006 to 31 st March, 2007	<u>365</u>
Total		<u>2557</u>

A satisfies 2nd additional condition also as his stay during 7 PYs immediately preceding relevant PY is more than 730 days.

Therefore, A is ROR in India during relevant previous year.

Illustration

A, for his business purposes, keep on commuting to and fro India. He leaves India on 18th April, 2013 and then comes back to India on 9th January, 2014. His stay in India during earlier years is as follows: 2012-13: Nil; 2011-12: 54 days; 2010-11: 162 days. Prior to this, he never went out of India. Determine his residential status.

Solution

Determination of Residential status of A for Previous Year 2013-14 (Assessment Year 2014-15):

In this case, both the basic conditions would be checked as A does not fall under any exception to basic conditions.

Stay of A in India during relevant PY 2013-14 = 1st April, 2013 to 18th April, 2013 (18 days) and 9th January, 2014 to 31st March, 2014 (23 + 28 + 31 days) = 100 days.

A does not satisfy 1st Basic condition. We will now check 2nd basic condition.

His stay during relevant PY is more than 60 days.

Stay during 4 PYs immediately preceding relevant PY:

PY	Stay Period in India	Days
2012-13	Nil	0
2011-12	Given	54
2010-11	Given	162
2009-10	1 st April, 2009 to 31 st March, 2010	365
Total		581

A satisfies 2nd basic condition as his stay during relevant PY is more than 60 days and during 4 PYs immediately preceding relevant PY is more than 365 days.

Therefore, A is Resident in India. Now, we will check additional conditions:

Additional Condition 1:

Resident in at least 2 PY out of 10 PYs:

PY	Falls under exception to basic condition	Stay during relevant PY (days)	First Basic Condition	Stay during 4 PY immediately preceding relevant PY (days)	Second basic condition	Residential status
2012-13	No	Nil	Not satisfied	Not required	Not satisfied	Non Resident
2011-12	No	54	Not satisfied	Not required	Not satisfied	Non Resident
2010-11	No	162	Not satisfied	1461 (365 + 365 + 366 + 365)	Satisfied	Resident
2009-10	No	365	Satisfied	Not required	Not required	Resident

A satisfies 1st additional condition as he is resident in at least 2 PYs out of 10 PYs immediately preceding relevant previous year.

Additional condition 2:

Stay of Individual in India during 7 PY immediately preceding relevant PY:

PY	Stay Period	Days
2012-13	Given	0
2011-12	Given	54
2010-11	Given	162
2009-10	1 st April, 2009 to 31 st March, 2010	365
2008-09	1 st April, 2008 to 31 st March, 2009	365
2007-08	1 st April, 2007 to 31 st March, 2008	366
2006-07	1 st April, 2006 to 31 st March, 2007	365
Total		1677

A satisfies 2nd additional condition also as his stay during 7 PYs immediately preceding relevant PY is more than 730 days.

Therefore, A is ROR in India during relevant previous year.

Illustration

A is an Indian citizen and is a practising advocate. He leaves India for his case in UK on 9th May, 2013. Determine his residential status.

Solution

Determination of Residential status of A for Previous Year 2013-14 (Assessment Year 2014-15):

In this case, both the basic conditions would be checked as A does not fall under any exception to basic conditions.

Stay of A in India during PY 2013-14: 1st April, 2013 to 9th May, 2013 : 39 days (30 + 9)

A does not satisfy 1st basic condition as his stay during relevant PY is less than 182 days.

A also does not satisfy 2nd basic condition as his stay during relevant PY is less than 60 days.

Therefore, A is Non Resident in India during relevant previous year.

Illustration

A is an Indian citizen. He goes for joining a company outside India on 18th September, 2013. His wife is resident and ordinary resident in India during previous year 2013-14. Determine his residential status.

Solution

Determination of Residential status of A for Previous Year 2013-14 (Assessment Year 2014-15):

A falls under exception to basic conditions as he goes for employment purposes outside India during relevant previous year. Therefore, in A's case only 1st basic condition would be checked.

Stay of A in India during PY 2013-14: 1st April, 2013 to 18th September, 2013 : 171 days (30 + 31 + 30 + 31 + 31 + 18 days)

A does not satisfy first basic condition as his stay during relevant PY is less than 182 days.

Therefore, A is Non Resident in India.

Note: Residential status of spouse is irrelevant for determining residential status of Individual.

Illustration

A is a foreign citizen. His father was born in Delhi in 1952 and his mother was born in England in 1953. His grandfather was born in Pakistan in 1917. He comes to attend his friends' marriage on 9th December, 2013 and stays in India for 261 days thereafter. Determine his residential status.

Solution

Determination of Residential status of A for Previous Year 2013-14 (Assessment Year 2014-15):

A falls under exception to basic conditions as he is a Person of Indian origin (as his grandfather was born in undivided India) and he comes on a visit to India during relevant PY. Therefore, in A's case, only 1st basic condition would be checked.

Stay of A in India during PY 2013-14: 9th December, 2013 to 31st March, 2014 : 113 days (23 + 31 + 28 + 31 days)

A does not satisfy first basic condition as his stay during relevant PY is less than 182 days.

Therefore, A is Non Resident in India.

2. RESIDENTIAL STATUS OF OTHER PERSONS (EXCEPT COMPANY): HUF, FIRM, AOP/BOI, LOCAL AUTHORITY, AJP

Determining Factor	Control and Management of the affairs of the business (from where major decisions relating to business are taken).
Resident	If Control and Management of the affairs of the business is wholly or partly in India.
Non-Resident	If Control and Management of the affairs of the business is wholly outside India.
ROR in case of HUF	If Karta of Resident HUF satisfies both the additional conditions as applicable in case of an Individual.
Additional Conditions	Karta should be resident in at least 2 PYs out of 10 PYs immediately preceding relevant PY; and Stay of Karta in India should be 730 days or more during 7 PYs immediately preceding relevant PY.

Illustration

AT & Co. (HUF) decisions are taken from India except 2 decisions which are taken from outside India. Determine residential status of HUF for AY 2014-15 assuming Karta of HUF is (a) ROR in India; (b) RNOR in India and (c) Non-Resident in India.

Solution

Determination of Residential status of AT & Co. (HUF) for Previous Year 2013-14 (Assessment Year 2014-15):

HUF is resident in India as control and management of its business affairs is partly situated in India (as some of its decisions are taken from India).

Now, it will be checked whether HUF is ROR or RNOR. It would depend upon satisfaction of additional conditions by Karta of HUF. If he satisfies both the additional conditions, then HUF would be ROR in India, otherwise HUF would be RNOR in India.

Case (a): HUF would be ROR in this case as Karta is ROR in India and he must be satisfying both the additional conditions.

Case (b): HUF would be RNOR in this case as Karta is RNOR in India and he would not be satisfying both the additional conditions.

Case (c): HUF in this case could be ROR or RNOR in India. If Karta is non-resident in India, his additional conditions are not yet checked. If he satisfies both the additional conditions, then HUF would be ROR and if he does not satisfy both the additional conditions, then HUF would be RNOR.

Illustration

AT & Co., a partnership firm is doing its business activities in India. However, meetings of its partners for decision making take place outside India except one, which has taken place in India. Determine Residential status of Partnership firm for AY 2014-15.

Solution**Determination of Residential status of AT & Co. for Previous Year 2013-14 (Assessment Year 2014-15):**

AT & Co., a partnership firm is resident in India as control and management of its business affairs is partly situated in India.

3. Residential status of Company

Indian Company	Always resident in India
Foreign Company	Residential status of a foreign company depends upon place of Control and Management (say, where meetings of Board of Directors are held) of its business affairs.
Resident	If Control and Management of its business affairs is wholly in India.
Non-Resident	If Control and Management of its business affairs is wholly or partly outside India.

Illustration

AT Ltd. is a company registered in India under the Companies Act, 1956. All its business activities are conducted outside India during relevant previous year. Further, all the meetings of the Board of directors are held outside India. Determine the residential status of AT Ltd. for the AY 2014-15.

Solution**Determination of Residential status of AT Ltd. for Previous Year 2013-14 (Assessment Year 2014-15):**

AT Ltd. is an Indian company as it is registered under the Companies Act, 1956.

AT Ltd. is therefore Resident in India as Indian companies are always resident in India.

Illustration

AT Inc. a company incorporated in USA, is carrying out certain business activities in India. All its decisions are taken in India except one decision which has been taken outside India. Determine the residential status of AT Inc. for the AY 2014-15.

Solution**Determination of Residential status of AT Inc. for Previous Year 2013-14 (Assessment Year 2014-15):**

AT Inc. is a foreign company as it is not registered in India. In its case, residential status depends upon control and management of its business affairs.

AT Inc. is Non-resident in India as control and management of its business affairs is partly situated in India.

Important Notes:

- It must be noted that only an individual or a HUF can be resident, not ordinarily resident or non-resident in India. All other assesses can be either resident or non-resident in India but cannot be not ordinarily resident in the matter of their residential status for all purposes of income tax.
- The expression control and management refers to the functions of decision-making and issuing directions but not the places where from the business is carried on.
- A person is deemed to be of Indian origin if he, or either of his parents or any of his grandparents, was born in Undivided India. It may be noted that grandparents include both maternal and paternal grandparents.

- The residential status of the assessee is to be determined each year with reference to the “previous year”. The residential status of the assessee may change from year to year. What is essential is the status during the previous year and not in the assessment year. Moreover, the concept of residential status is nothing to do with nationality or domicile of a person. An Indian, who is a citizen of India, can be non-resident for Income Tax purposes, whereas a foreigner can be resident of India for Income Tax purpose.

SCOPE OF TOTAL INCOME [SECTION 5]

Section 5 provides the scope of the total income of the assessee because the incidence of tax on any person depends upon his residential status. The scope of total income of an assessee depends upon the following three important considerations:

- the residential status of the assessee.
- the place of accrual or receipt of income, whether actual or deemed and
- the point of time at which the income had accrued to or was received by or on behalf of the assessee.

Tax incidence vis-a-vis residential status of all assesses is indicated in the following table.

<i>Where tax incidence arises in case of</i>	<i>Resident or Resident & Ordinarily Resident</i>	<i>Resident but not Ordinarily Resident (only Individual or HUF)</i>	<i>Non-Resident</i>
Income received in India (Whether accrued in or outside India)	TAXABLE	TAXABLE	TAXABLE
Income deemed to be received in India (Whether accrued in or outside India)	TAXABLE	TAXABLE	TAXABLE
Income accruing or arising in India (Whether received in India or outside India)	TAXABLE	TAXABLE	TAXABLE
Income deemed to accrue or arise in India (Whether received in India or outside India)	TAXABLE	TAXABLE	TAXABLE
Income received and accrued outside India from a business controlled or a profession set up in India	TAXABLE	TAXABLE	NOT TAXABLE
Income received and accrued outside India from a business controlled from outside India or a profession set up outside India	TAXABLE	NOT TAXABLE	NOT TAXABLE
Income earned and received outside India but later on remitted to India (whether tax incidence arises at the time of remittance)	NOT TAXABLE	NOT TAXABLE	NOT TAXABLE
Dividend from an Indian Company of Mutual Fund specified under Section 10(23D)	EXEMPT U/S 10(34) and 10(35)		
Agricultural Income in India	EXEMPT U/S 10(1)		

Long term capital gain (on securities on which Securities transaction tax is paid)	EXEMPT U/S 10(38)
Past untaxed profits (of earlier years)	NOT TAXABLE
Remittances (Second receipt) to India	NOT TAXABLE
Gifts from relative (on any occasion) or Gift on marriage from any person	NOT TAXABLE

Note

(i) Income is accrued or arise at a place where source of Income is situated. For example, for salary income, source is situated at the place where services are rendered.

(ii) **Income deemed to accrue or arise in India [Section 9]:**

1. Income from a business connection (in the form of branch office, project office, agent etc.) in India will be deemed to accrue or arise in India.

Exceptions:

- Income from a business connection will be deemed to accrue or arise in India only to the extent of profits attributable to operations in India. Say, if 10% Weightage is given to work in India, then only 10% of the profits would be deemed to accrue or arise in India.
- Purchase of goods by a NR for the purpose of export will not be deemed to be business connection in India;
- Collection of news and views by a news channel or news agency etc. in India will not be deemed to be a business connection in India;
- Shooting of films in India provided: If maker is individual, he should neither be an Indian citizen nor be Resident in India; if maker is Firm/AOP etc., then none of its members/partners should be Indian citizen or Indian resident; if maker is company, then none of its shareholders should be Indian citizen or Indian resident.

2. Income from any property, asset or source of income situated in India
3. Income from the transfer of any capital asset situated in India
4. Any income under the head 'Salaries' if it is payable for services rendered in India
5. Salary payable by the Government to an Indian Citizen for services rendered outside India
6. Interest payable by:
 - Government;
 - Resident except where interest is payable in respect of borrowings used for business or profession outside India or for earning any income from any source outside India;
 - Non-Resident if interest is payable in respect of borrowings used for a business or profession in India.
7. Royalty payable by:
 - Government;
 - Resident except where it is payable in respect of any right/information/property used for the purpose of a business or profession outside India or earning any income from any source outside India;
 - Non-Resident if royalty is payable in respect of any right/information/property used for the purpose of business or profession in India or earning any income from any source in India.

8. Fees for technical services payable by:

- Government;
- Resident except where services are utilised for a business or profession carried on outside India or earning any income from any source outside India; or
- Non-Resident if fee is payable in respect of services for a business or profession carried on in India or earning any income from any source in India.

Illustration

Details of incomes of Mr. A for the financial year 2013-14 is as follows:

- (a) He works in an Indian Company and receives salary in India during the year ₹ 3,60,000.
- (b) He has a house in Delhi from which he has earned Income from house property amounting to ₹ 2,70,000. Rental income is received in Japan.
- (c) He has received dividend of ₹ 90,000 from TCS Ltd., an Indian company and has also received dividend of ₹ 63,000 (equivalent Indian rupees) from a foreign company outside India.
- (d) He transfers shares of an Indian company outside India to a Non resident individual and earns a short term capital gain of ₹ 45,000.
- (e) He has also earned a long term capital gain of ₹ 72,000 by sale of shares on stock exchange in India, on which securities transaction taxes have been paid.
- (f) He has rendered technical services to a company outside India, which has used these services for its business outside India. Income received outside India is ₹ 1,80,000.
- (g) Royalty of ₹ 4,50,000 received from providing know-how, which is utilised by a foreign company in India.
- (h) Interest received from Government of India is ₹ 18,000.
- (i) Past untaxed profits of financial year 2009-10 are ₹ 5,40,000.
- (j) He earns and receives rental income of ₹ 9,00,000 outside India. Out of this, ₹ 7,20,000 is remitted to India. Remaining amount is spent for education of the children abroad.
- (k) He got married in the current year and has received ₹ 81,000 in cash gift from his friends. He also got a gift on his birthday in June from his wife's father ₹ 27,000. He also gifts worth ₹ 63,000 from his friends on his birthday.
- (l) He has also earned an agricultural income in India of ₹ 1,23,300.
- (m) He is doing a business in Sri Lanka but it is controlled from Delhi. Income of ₹ 1,80,000 is earned in that business.
- (n) He is doing a business in Japan from which he receives an income of ₹ 42,300.

Compute the total income in case of Mr. A for Assessment Year 2014-15 assuming he is (i) Resident and Ordinary Resident; (ii) Resident but not ordinary resident; (iii) Non-resident.

Solution

Computation of Total Income of Mr. A for Assessment Year 2014-15 (Previous Year 2013-14)

Particulars	ROR	RNOR	NR
(a) Salary received in India (Income received in India)	3,60,000	3,60,000	3,60,000
(b) Rent from a house property in Delhi (Income deemed to accrue or arise in India)	2,70,000	2,70,000	2,70,000
(c) Dividend from TCS Ltd., an Indian company [Exempt u/s 10(1)]	-	-	-

Dividend from a foreign company (Income accrued or arise outside India)	63,000	-	-
(d) Short term capital gain on sale of shares of an Indian company (Income deemed to accrue or arise in India)	45,000	45,000	45,000
(e) Long term capital gain (on STT paid securities) [Exempt u/s 10]	-	-	-
(f) Fees for technical services used for purposes outside India (Income accrued or arise outside India)	1,80,000	-	-
(g) Royalty from a foreign company for right used in India (Income deemed to accrue or arise in India)	4,50,000	4,50,000	4,50,000
(h) Interest received from Government of India (Income deemed to accrue or arise in India)	18,000	18,000	18,000
(i) Past untaxed profits of FY 2009-10 (Not taxable in current year)	-	-	-
(j) Rental income outside India (Income accrued or arise outside India)	9,00,000	-	-
Note: Remittance (second receipt) and use of money for education of children is irrelevant.			
(k) Gift on the occasion of marriage (not taxable)	-	-	-
Gift on birthday from relative (not taxable)	-	-	-
Gift on birthday from other than relatives (taxable if amount exceeds ₹50,000)	63,000	63,000	63,000
(l) Agricultural income in India [Exempt u/s 10(l)]	-	-	-
(m) Income from business in Sri Lanka controlled from India (Income accrued or arise outside India from a business controlled from India)	1,80,000	1,80,000	-
(n) Income from business in Japan (Income accrued or arise outside India)	42,300	-	-
Total Income	25,71,300	13,86,000	12,06,000

VARIOUS HEADS OF INCOME

The taxability of income of a person depends on the chargeability of such income under the Income tax Act 1961. The total income of an assessee (subject to statutory exemptions) is chargeable under Section 4(1).

The total income chargeable to income tax is divided into 5 heads of income. Section 14 enumerates the five head of income as follows:

(A) Salaries: Income arising in the hands of an employee by way of salary, pension, bonus allowances and other benefits will fall under the head salaries.

(B) Income from house property: Income in the form of rental income by letting out a house property is taxable under the head "Income from house property".

(C) Profits and gains of business or profession: Income derived from carrying on any business or profession is taxable under the head "Profits and gains from business or profession".

(D) Capital gains: Profit from transfer of a capital asset is taxable under the head “Capital Gains”.

(E) Income from other sources: This is a residuary head of income. The income which does not fall under the four heads of income will be taxable as income from other sources.

INCOME UNDER THE HEAD SALARIES (SECTION 15 TO 17)

The RELATIONSHIP of PAYER AND PAYEE must be of employer and employee for an income to be categorized as salary income. As such the existence of “employer-employee” relationship is the “sine-qua-non” for taxing a particular receipt under the head salaries. It does not matter whether the employee is a full time employee or a part-time one. Once the relationship of employer and employee exists, the income is to be charged under the head “salaries”.

As per Section 15, the income chargeable to income tax under the head salaries would include :

- Any salary due to an employee from an employer or a former employer during the previous year irrespective of the fact whether it is paid or not.
- Any salary paid or allowed to the employee during the previous year by or on behalf of an employer, or former employer, would be taxable under this head even though such amounts are not due to him during the accounting year.
- Arrears of salary paid or allowed to the employee during the previous year by or on behalf of an employer or a former employer would be chargeable to tax during the previous year in cases where such arrears were not charged to tax in any earlier year.

In short, salary is chargeable to tax on DUE OR RECEIPTS BASIS, whichever is earlier.

- (i) Due basis – when it is earned even if it is not received in the P.Y. (Accrued)
- (ii) Receipt basis – when it is received even if it is not earned in the P.Y. (Advance)

The following format for Computation of Salary will provide a comprehensible summary of the whole head of income:

Particulars	Details	Amount
Basic Salary		*****
Fees		*****
Commission		*****
Bonus (on receipt basis)		*****
Gratuity		*****
Leave Encashment		*****
Pension		*****
Retrenchment Compensation		*****
Compensation received under Voluntary Retirement Scheme		*****
<u>Allowances:</u>		
Dearness Allowance (DA) /Dearness Pay (DP)		*****
House Rent Allowance		*****
Children Education Allowance		*****
Hostel Expenditure Allowance		*****
Entertainment Allowance		*****
Medical Allowance		*****

Conveyance Allowance	*****
City Compensatory Allowance	*****
Uniform Allowance	*****
Professional Development Allowance	*****
Transport Allowance	*****
Other Allowances	*****
Perquisites u/s 17(2)	*****
Any Obligation of Employee paid by Employer	*****
Accommodation	*****
Shares and securities issued under ESOP	*****
Employer's Contribution to Superannuation Fund in excess of ₹1,00,000/-	*****
Insurance premium	*****
Medical Facility	*****
Other fringe benefits	*****
Leave Travel Concession	*****
Contribution of Employer to Provident Fund	*****
Interest on Recognized Provident Fund	*****
Any other item	*****
Gross Salary	*****
<i>Less : Deduction u/s 16</i>	
Entertainment Allowance[Section 16(ii)]	***
Tax on employment/Professional tax [section 16(iii)]	***
Taxable Salary	****

The above items are discussed in brief as follows:

1. ALLOWANCES

Allowance means the fixed sum paid by employer to employee to meet official or personal expenses.

Fully exempted allowances

- (a) Allowances to an Indian citizen employed abroad by Government of India;
- (b) Allowances to High Court Judges;
- (c) Sumptuary (in the nature of entertainment allowance) allowance given to High Court and the Supreme Court Judges;
- (d) Allowances received by an employee of United Nations Organisation (UNO).

Partially exempt or fully exempt allowances on satisfaction of the prescribed conditions [Section 10(14)]

(1) Certain allowances are exempt upto the amount spent for specified purposes i.e. exemption would be lower of the actual allowance or amount spent for specified purposes – Transfer allowance, Helper allowance, Academic allowance, Research or Research and Development allowance, Daily allowance, Uniform allowance, Conveyance allowance and Travelling Allowance.

Example: If suppose employer provides a uniform allowance of ₹36,000 during the year for purchase and maintenance of uniform and employee spends ₹27,000 for purchase and maintenance of uniform, then exemption would be ₹27,000 and remaining ₹9,000 would be taxable uniform allowance.

(2) Certain allowances are exempt upto the amount specified by Government i.e. exemption would be lower of the actual allowance or amount specified by Government.

- Transport allowance: Exempt upto ₹800 pm (1600 pm for blind or orthopaedically handicapped);
- Children education allowance: Exempt up to ₹100 pm per child for maximum of 2 children;
- Hostel allowance: Exempt upto ₹300 pm per child for maximum of 2 children;
- Special allowance to employees working in Transport systems: Exempt upto lower of ₹10,000 pm or 70% of the allowance.
- Tribal area allowance: Exempt upto ₹200 per month.
- Certain other allowances: High altitude (uncongenial climate) allowance etc. are exempt on the basis of range specified in rules.

(3) House Rent Allowance [Section 10(13A) and Rule 2A]: Least of the following is exempt:

- 50% of Superannuation salary (SAS) in case of Delhi, Mumbai, Kolkata, Chennai; 40% in case of other cities
- Rent paid – 10% of SAS;
- Actual HRA

Taxable HRA = Actual HRA – Exemption

Meaning of SAS: Basic Salary + Dearness Allowance (forming part of salary for retirement benefits) + % commission on Turnover

Fully Taxable Allowances

All allowances other than covered above, e.g. Servant, City Compensatory, Overtime, Project, Entertainment, Dearness, Rural, Absent, Fixed Medical, Tiffin, High Cost of Living, Holiday Home, Marriage, Telephone Allowance are taxable allowances.

PERQUISITES

Perquisites are the benefits or amenities in cash or in kind, or in money or money's worth and also amenities which are not convertible into money, provided by the employer to the employee whether free of cost or at a concessional rate. Their value, to the extent these go to reduce the expenditure that the employee normally would have otherwise incurred in obtaining these benefits and amenities, is regarded as part of the taxable salary.

Free or Concessional Accommodation Facility - Taxable for all employees

A. Unfurnished accommodation

- Government Employee: Taxable value of perquisite is the License fee as per Government Rules minus Recovery, if any.
- Non-Government Employees:
 - Accommodation owned by employer:* Taxable value of perquisite depends upon population of city as per the latest census:

- If Population is upto 10 Lakhs: Taxable value is 7.5% of salary minus recovery, if any;
- If Population exceeds 10 lakhs but is upto 25 lakhs: Taxable value is 10% of salary minus recovery, if any;
- If Population exceeds 25 lakhs: Taxable value is 15% of salary minus recovery, if any.

(b) *Accommodation hired by employer*: Taxable value is lower of 15% of salary or actual hire charges paid **minus** Recovery, if any, to be deducted from above.

Salary = Basic + DA (forming part of salary for retirement benefits) + any commission + bonus due + fees + taxable portion of all allowance (from all employers for the period of accommodation)

B. Furnished Accommodation

Taxable Value = Value of Unfurnished house + Value of Furniture

- Value of Furniture:
- (i) If owned by employer: 10% of original cost
 - (ii) If hired by employer: Hire charges paid by employer
Recovery, if any would be deducted.

C. Hotel Accommodation

Taxable Value: Lower of 24% of salary or hire charges paid for the period of accommodation in the hotel. Recovery, if any, is to be deducted.

This perquisite would not be taxable if hotel accommodation is provided for up to 15 days on transfer.

Other perquisites taxable for all employees:

- (1) Life Insurance Premium: Premium payable is taxable in the hands of all employees.**
- (2) Obligation of employee met by employer: Taxable on paid basis in the hands of all employees.**
- (3) Sale of Moveable assets:**

Taxable Value = Cost – Depreciation for each completed year of asset – recovery

Depreciation Rates (for completed years only):

- Computer – 50% WDV (Written down value) method
- Motor Car – 20% WDV
- Other Assets – 10% SLM (Straight line method)

Note: Sale of Stock to employee is not taxable.

(4) Use of Movable Asset:

- If owned by employer: 10% of original cost
- If hired by employer: Hire charges paid by employer

Recovery, if any would be deducted from above.

Note: Use of telephone, mobile, laptop and computer is not taxable.

(5) Gifts: If received in cash from employer on any occasion, then such gift shall be fully taxable and if it is in kind then it is exempt upto ₹ 5000 and any amount beyond ₹ 5,000 would be taxable.

(6) Credit card facility: Actual expenditure incurred is taxable. Expenditure incurred for official purposes is not taxable. Proper record is to be maintained for claiming exemption i.e. Details of the expenditure incurred

along with purpose, date etc. and Employer's certificate to the effect that the expenditure has been incurred wholly and exclusively for official purposes.

(7) Club facility: Actual expenditure incurred is taxable. Expenditure incurred for official purposes is not taxable. Proper record is to be maintained for claiming exemption.

Note: Health club facility uniformly for all employees is exempt. Corporate membership is exempt.

(8) Holiday home facility: Actual expenditure incurred is taxable. Market fees is taxable if not provided to all employees. Official tour of employee is exempt. Family member's tour or extended vacation is taxable. Recovery, if any, would be deducted.

(9) Meals: Actual expenditure incurred is taxable. However, ₹ 50 per meal, refreshments (snacks and non-alcoholic beverages provided during working hours including extended working hours or working on holidays) and meals in remote area or offshore installation are exempt.

(10) Employees Stock Options (ESOPs): Fair Market Value on exercise date less recovery if any shall be taxable.

The ESOPs are taxable as perquisites in the hands of employees. There are three stages in Employees Stock Option plan i.e.

Stage 1: When the employee is offered shares under ESOP.

Stage 2: After completing a time period of service, say three years, the employee can exercise the option to get ESOPs (Acceptance of ESOPs)

Stage 3: The company allots ESOPs (Allotment of ESOPs).

It may be noted that:

Perquisite shall be taxable in the hands of the employee only when shares are allotted to him under ESOPs. The perquisite is not taxable when employee exercises his option to ESOPs. However, perquisite shall be worked out on the basis of Fair Market value of ESOPs on the date when employee exercises his option to ESOPs.

Determination of Fair Market Value (FMV) of ESOPs on the date of exercise of option:

- (a) Where shares in the company are listed on a single stock exchange: FMV will be average of opening and closing prices of shares on the date of exercise of option.

If on the date of exercise of option there is no trading in shares, the FMV shall be the closing price of the share on any recognised stock exchange on a date closest to the date of exercise of option and immediately preceding such date of exercise of option.

- (b) Where shares in the company are listed on more than one recognised stock exchange: FMV will be average of opening and closing price of shares on the date of exercise of option on a recognised stock exchange which records the highest volume of trading in the shares.

If on the date of exercise of option there is no trading in shares, the FMV shall be the closing price of the share on a recognised stock exchange which records the highest volume of trading on a date closest to the date of exercise of option and immediately preceding such date of exercise of option.

- (c) Where shares in the company are not listed on a recognised stock exchange: FMV will be value on a "specified date" as determined by a Category I merchant banker registered with SEBI.

Specified date means the date of exercise of option or any date earlier than the date of exercise of option, not being a date which is more than 180 days earlier than the date of exercise of option.

Notes:

- (i) **Period of Holding [Section 2(42A)]:** In the case of a capital asset, being any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer free of cost or at concessional rate to his employees (including former employee or employees), the period shall be reckoned from the date of allotment or transfer of such specified security or sweat equity shares.
- (ii) **Cost of Acquisition [Section 49(2AA)]:** Where the capital gain arises from the transfer of specified security or sweat equity shares referred to in section 17(2)(vi), the cost of acquisition of such security or shares shall be the FMV which has been taken into account for the purposes of the said section.

Illustration

A is employed by an Indian subsidiary company of a foreign holding company. ESOP shares are issued by the foreign holding company to A at a pre determined price of ₹ 90 per share. On the date of vesting, fair market value of foreign holding company's shares is ₹ 900 per share. On the date of allotment, the fair market value is ₹ 1,170 per share. While during the grant period, A was not based in India at all, he was based in India on 10th June, 2013 when shares were allotted to him. What will be the cost of acquisition of shares in the hands of A? Can A claim any deduction in respect of pre-determined price of ₹ 90 per share which is paid by him to get the allotment of shares?

Solution

Taxable value of perquisite in the hands of employee: FMV on the exercise date minus recovery if any from employee.

In the present case FMV on the exercise date is ₹ 900 per share and shares are offered to employee at ₹90 per share, therefore, ₹ 810 per share being the difference of two prices would be treated as taxable value of the perquisite in the hands of an employee. Deduction of ₹ 90 per share is allowed from the FMV to arrive at the taxable value.

As per section 49(2AA), cost of acquisition of shares in the hands of employee would be the FMV on the exercise date. Therefore, in the present case, cost of acquisition of shares in the hands of A would be ₹ 900 per share.

Perquisite Taxable in case of specified employees only (Taxable in case of all employees if it is in the nature of an obligation of employee met by employer)

What is Specified employee?

Specified employee includes Director of a company or a person holding substantial interest (20% or more share in profits or voting rights) in a company or concern or a person having cash taxable salary of more than ₹ 50,000 per annum.

Cash taxable salary = Basic + Dearness Allowances + All taxable allowances + All other amounts received in cash.

The following perquisites received by the specified employees shall be taxable:

(1) Gas/Electricity/Water Facility

- (i) If provided from own sources: Manufacturing cost for the units consumed
- (ii) Others: Cost incurred by employer

Recover, if any would be deducted.

(2) Education Facility

- (i) If school or institution owned and maintained by employer:
 - Market fee (in similar institution) – Exemption of ₹ 1,000 pm per child
- (ii) If other schools/institutions, actual cost incurred is taxable. Recovery, if any, would be deducted.

Nothing shall be taxable for the amount incurred on training of employees and Scholarship.

(3) Medical Facility

(i) In India

- (a) In employer's hospital: Nothing shall be taxable
- (b) In Govt. hospital: Nothing shall be taxable
- (c) In approved hospital: Nothing shall be taxable
- (d) Others: Not taxable up to ₹15,000

(ii) Outside India:

- (a) Boarding/Lodging expenses of patient and one attendant shall be exempted to the extent specified by RBI.
- (b) Treatment expenses shall be exempted upto the extent specified by RBI
- (c) Travelling expenses of patient and one attendant shall be fully exempted if total income (excluding this facility) of employee is upto ₹2 lakhs p.a. Otherwise, fully taxable.

(4) Servant facility: Actual cost incurred by the employer shall be taxable less recovery, if any.

(5) Car Facility

(i) Car owned by employer and expenses borne by employer

- (a) Personal use: All expenses + 10% of cost for depreciation + salary of driver – Recovery.
- (b) Official use: nil (if specified documents are maintained)
- (c) Personal and official use both:
 - Small Car: ₹1800 pm + 900 pm for driver is taxable
 - Big Car: ₹2400 pm + 900 pm for driver is taxable

Note: Small Car (Car with Cubic Capacity upto 1.6 litres) and Big Car (Cubic Capacity more than 1.6 litres)

(ii) Car owned by employer and expenses borne by employee

- (a) Personal use: 10% of cost for depreciation + salary of driver (if borne by employer) – Recovery.
- (b) Official use: nil (if specified documents are maintained)
- (c) For personal and official use both:
 - Small Car – 600 pm + 900 pm for driver is taxable
 - Big Car – 900 pm + 900 pm for driver is taxable

(iii) Car owned by employee and expenses borne by employer

- (a) Personal use: All expenses + salary of driver – Recovery.
- (b) Official use: nil (if specified docs are maintained)
- (c) For personal and official use both:
 - Small Car: 1800 pm + 900 pm for driver is exempt
 - Big Car: 2400 pm + 900 pm for driver is exempt

Exempted perquisites

The following are the exempted perquisites for all employees:

- Staff Group insurance
- Use of laptop, computer and telephone
- Gifts upto ₹ 5000 in kind
- Sale of Stock
- Sale of asset which is 10 year or more old
- Interest free loan or concessional loan not exceeding ₹ 20,000
- Loan facility for treatment of specified diseases
- Credit card/club if given for official purpose is exempt
- Health club – for all employees is exempt
- Corporate membership – Initial fees is exempt
- Holiday home facility – official purpose is exempt
- Meal upto ₹ 50 per meal is exempt
- Meal in remote area is exempt
- Hotel accommodation – transfer and upto 15 days
- Education facility upto ₹1000 per month per child
- Training of employees is exempt
- Scholarship is exempt
- Medical facilities upto ₹ 15,000 in private hospitals is exempt
- Medical facilities in own/Govt. hospital is exempt
- Medical treatment of specified disease in an approved hospital.

GRATUITY (AWARD FOR LONG TERM SERVICE) [EXEMPTION U/S 10(10)]

The following are the provisions for taxability of gratuity received from the employer:

(i) Government Employees: Gratuity received by the government employees shall be fully exempt.

(ii) Other than Government employees:

- (a) Employees covered by payment of Gratuity Act:** In this case the least of following shall be exempt:
- 15/26 (×) Salary at the time of retirement (×) Completed years of service
 - ₹10,00,000
 - Actual Gratuity received

Note:

- 7/26 shall be taken in case of seasonal establishment. [7 days salary in case of seasonal establishment]
- Salary = Basic + 100% of Dearness Allowance at time of retirement
- Part of year in excess of 6 months considered as full year.

(b) Employees not covered by payment of Gratuity Act: In this case least of following shall be exempt:

- $1/2 \times \text{Average salary} \times \text{Completed years of service}$
- ₹ 10,00,000
- Actual Gratuity received

Note:

- o Average Salary of last 10 months preceding the month of retirement will be taken,
- o Salary = Basic + DA (if forms part of salary) + % commission if as per the terms of employment
- o Fraction of year is ignored.
- o If exemption allowed earlier, then ₹10,00,000 would reduce by exemption allowed earlier.

Gratuity during employment is fully taxable.

PENSION

Following are the provisions for taxability of amount of pension:

- (i) **Uncommuted Pension:** Fully taxable for all employees, whether Government or non-Government.
- (ii) **Commutted (Lump-sum)**
 - (a) **Government employee:** The amount of commuted pension shall be fully exempt
 - (b) **Non-Government employee receiving gratuity:** $1/3^{\text{rd}}$ of full value of pension shall be exempt.
Full value: commuted pension divided by % age of commuted multiplied by 100
 - (c) **Non-Government employee not receiving gratuity:** $1/2$ of full value of pension shall be exempt.

LEAVE SALARY/ENCASHMENT [EXEMPTION U/S 10(10AA)]

Following are the taxability provisions pertaining to encashment of leaves or leave salary:

(i) During employment: If the leave salary is received during the service, then the amount received shall be fully taxable for everyone

(ii) On Retirement:

- (a) **Government employee: Fully exempt**
- (b) **Non – Government employee:** In this case least of following shall be exempt
 - Earned leave \times Average monthly salary
 - $10 \times$ Average monthly salary
 - ₹3,00,000
 - Actual leave salary received

Note: Earned Leave = Leave entitlement (leave entitlement as per service rule or 30 days for each completed years of service \times completed years of service ignoring part of year) – leave availed in service – leave encashed during service

Average salary = Salary of last 10 months preceding the date of retirement will be taken

Salary = Basic + DA (forming part of salary) + % commission if in terms of employment

If exemption allowed earlier than ₹ 3,00,000 would reduce by exemption allowed earlier.

TREATMENT OF PROVIDENT FUNDS

Statutory Provident Fund: Following are the provisions with regards to statutory provident fund:

(I) Periodic Contribution and Interest:

- Employer's Contribution: Exempt
- Employee's contribution: Not taxable and eligible as deduction under section 80C.
- Interest on outstanding balance: Exempt

(II) Lump sum receipt on retirement/death:

- Employer's Contribution: Exempt
- Employee's contribution: Not taxable.
- Interest on Employer's contribution: Exempt
- Interest on Employee's contribution: Exempt

Recognised Provident Fund: Following are the provisions with regards to Recognised Provident Fund:

(I) Periodic Contribution and Interest:

- Employer's Contribution: Exempt upto 12% of salary [Basic + DA (part of salary) + % commission on turnover]
- Employee's contribution: Not taxable and eligible as deduction under section 80C.
- Interest on outstanding balance: Exempt upto 9.5% p.a.

(II) Lump sum receipt on retirement/death (provided employee is in continuous service for 5 years, otherwise fully taxable):

- Employer's Contribution: Exempt
- Employee's contribution: Not taxable.
- Interest on Employer's contribution: Exempt
- Interest on Employee's contribution: Exempt

Unrecognised Provident Fund: Following are the provisions with regards to Unrecognised Provident Fund:

(I) Periodic Contribution and Interest:

- Employer's Contribution: Not taxable.
- Employee's contribution: Not taxable.
- Interest on outstanding balance: Not taxable

(II) Lump sum receipt on retirement/death:

- Employer's Contribution: Taxable as Salary
- Employee's contribution: Not taxable.
- Interest on Employer's contribution: Taxable as Salary
- Interest on Employee's contribution: Taxable as Income from other sources.

DEDUCTION U/S 16

(I) Entertainment Allowance [Section 16(ii)]: Deduction of the least of the following shall be allowed to

Government Employees only;

- 20% of basic salary;
- ₹5000
- Actual allowance

(II) Professional Tax [Section 16(iii)]: Deduction is allowed in the year of payment. If paid by employer, then first include in salary as a perquisite and then a deduction shall be allowed.

Illustration

T has retired on 31st December, 2013 after serving 27 years, 9 months and 18 days, from AT Ltd. a company based out of Gurgaon, Haryana. She has received the following emoluments during previous year 2013-14:

- (a) Basic Salary upto 30th June, 2013 was ₹ 27,000 and subsequently it was increased to ₹ 30,600 per month.
- (b) Dearness allowance received by T was 30% of basic salary.
- (c) AT Ltd. is into transport business. T has received a special transport allowance of ₹ 13,500 per month as she has to remain out of home for her job. She spends ₹ 10,800 per month for meeting her expenditure.
- (d) She receives City Compensatory Allowance of ₹ 1,800 per month and she also receives pet allowance of ₹ 900 per month.
- (e) She was provided a concessional accommodation at Delhi which was taken on lease by employer at a rent of ₹ 9,000 per month. Along with this, furniture costing ₹ 1,08,000 was also provided to her. Book value of furniture was ₹ 64,800. Employer charged ₹ 1,000 per month from her for the accommodation.
- (f) She has also received gratuity amounting to ₹ 7,00,200 on retirement. She was covered under the payment of gratuity act.
- (g) She received leave encashment of ₹ 4,05,000 on retirement. She was allowed 1.5 month for every year of service. She availed 18 months leave during her employment.
- (h) Her pension at the time of retirement was fixed at ₹ 18,000 per month. However, she got 50% of this pension commuted and got ₹ 6,30,000 on 1st March, 2014.
- (i) Her employer has contributed ₹ 54,360 during the relevant year to unrecognised provident fund (URPF). She had also contributed an equal amount. She received her accumulated balance of ₹ 854,100 from URPF on retirement, out of which ₹ 3,00,600 was for interest and balance was equal contribution from employer and employee.
- (j) Employer reimburses medical bills of ₹ 27,450 of employee during the previous year.
- (k) Employer also reimbursed for medical treatment of a household member of employee outside India. Expenses incurred were: ₹ 27,00,000 on treatment outside India, Boarding and lodging of patient and one attendant: ₹ 4,50,000 and travelling expenses of patient and one attendant ₹ 1,44,000. Amount permitted by RBI for treatment was ₹ 24,30,000 and for boarding and lodging, it was ₹ 3,78,000.
- (l) Employer has provided education to two children of employee as well as dependent brother of T in an institution owned and maintained by him. The total fee per child amounted to ₹ 45,000 for the period of employment. The cost of education in similar institution was ₹ 54,000 per child.
- (m) Employer has also incurred an amount of ₹ 80,550 on leave travel concession to employee for travelling from Delhi to Kanyakumari. By the shortest route, this amount comes to ₹ 70,560.
- (n) Determine the Total Income and tax liability of T for the AY 2014-15 assuming she is of 60 years of age.

Solution**Computation of Total Income of T for the Assessment Year 2014-15**

Sl. No.	Particulars	Amount (₹)
(a)	Basic Salary (fully taxable) $[27,000 \times 3 + 30,600 \times 6]$	2,64,600
(b)	Dearness allowance (fully taxable) [30% of basic salary)	79,380
(c)	Special transport allowance (exempt upto lower of 70% of the allowance or ₹ 10,000 per month) $[(13,500-9,450) \times 9]$	36,450
(d)	City Compensatory Allowance (fully taxable) $[1800 \times 9]$	16,200
	Pet allowance (fully taxable) $[900 \times 9]$	8,100
(e)	Taxable value of concessional accommodation (Working note 1)	47,903
(f)	Taxable gratuity (Working note 2)	57,600
(g)	Leave encashment on retirement (Working note 3)	1,42,560
(h)	Pension:	
	– Uncommitted (Working note 4)	45,000
	– Commuted (Working note 4)	2,10,000
(i)	Employer's contribution to URPF (not taxable)	Nil
(i)	Lump-sum receipt from URPF at the time of retirement:	
	– Employer's contribution to URPF(Working note 5)	2,76,750
	– Interest on employer's contribution (Working note 5)	1,50,300
(k)	Medical facility in India in private clinic/reimbursement etc. (not taxable upto ₹ 15,000) $[27,450-15,000]$	12,450
(l)	Medical facility outside India:	
	– Medical treatment of patient (exempt upto the extent specified by RBI) $(27,00,000-24,30,000)$	2,70,000
	– Boarding and lodging expenses of patient and one attendant (exempt upto the extent specified by RBI) $(4,50,000-3,78,000)$	72,000
	- Travelling expenses of patient and one attendant (fully taxable as employees' total income before including this perquisite exceeds ₹ 2,00,000)	1,44,000
(m)	Education facility in an institution owned/maintained by employer (Taxable value is actual cost in similar institution – ₹ 1,000 per month per child for employee's children only – Recovery, if any) $[54,000 \times 3-1,000 \times 9 \times 2]$	1,44,000
(n)	Leave travel concession in India (exempt upto the amount spent on travel by the shortest route) $[80,550-70,560]$	<u>9,990</u>
	GROSS SALARY	19,87,283
	Less: Deductions under section 16	<u>Nil</u>
	NET SALARY	19,87,283
	Add: Income from other sources:	
	– Interest received on employee's contribution to URPF	<u>1,50,300</u>
	GROSS TOTAL INCOME	21,37,583
	Less: Deductions under section 80C to 80U	<u>Nil</u>
	TOTAL INCOME	21,37,583
	TOTAL INCOME (ROUNDED OFF)	21,37,580

Computation of tax liability of Ms. T for the Assessment Year 2014-15 (Previous Year 2013-14)

Particulars	Amount (₹)
Tax liability $[(21,37,580 - 10,00,000) \times 30\% + 1,25,000]$	4,66,274
<i>Add:</i> Surcharge, if any	Nil
Tax including surcharge	4,66,274
<i>Add:</i> Education cess @ 2% (on tax including surcharge)	9,325
<i>Add:</i> Secondary and Higher education cess @ 1% (on tax including surcharge)	<u>4,663</u>
Total tax liability	4,80,262
<i>Less:</i> Taxes paid	Nil
Tax payable	4,80,262
Tax payable (rounded off)	<u>4,80,260</u>

Working Notes:**(1) Value of Concessional Furnished accommodation:**

Taxable value = Value of rent free unfurnished house + Value of furniture – Recovery, if any.

Value of rent free unfurnished house = Lower of 15% of salary or lease rent paid by employer

Lease rent = $9,000 \times 9 = ₹ 81,000$.

Meaning of Salary for above purpose:

	₹
Basic Salary	2,64,600
Dearness allowance (assumed nothing forms part of salary)	Nil
Taxable special transport allowance	36,450
Taxable City compensatory allowance	16,200
Taxable Pet allowance	<u>8,100</u>
Salary for Rent Free Accommodation	<u>3,25,350</u>

15% of Salary = ₹ 48,803

Therefore, Value of unfurnished house = ₹48,803.

Value of furniture = 10% p.a. of original cost as furniture is owned by the employer = $1,08,000 \times 10\% \times 9/12 = ₹ 8,100$

Value of concessional accommodation = $48,803 + 8,100 - 9,000 = ₹ 47,903$

(2) Taxable Gratuity:

Exemption is provided under section 10 to the extent of following (employee is covered by the payment of gratuity act):

Rule 1: $15/26 \times \text{completed years of service} \times \text{salary at the time of retirement} = 15/26 \times 28 \times (30,600 + 9,180) = ₹ 6,42,600$

Rule 2: ₹10,00,000

Rule 3: Actual gratuity = ₹7,00,200

Exemption = ₹6,42,600

Taxable Gratuity = Amount of gratuity – exemption = ₹57,600

(3) Taxable Leave encashment :

Exemption is provided under section 10 to the extent of following:

Rule 1: Earned leave \times Average monthly salary

Earned leave = Leave entitlement (lower of 1 month or 1.5 month as per service rule for every completed year of service) – Leave availed = $1 \times 27 - 18 = 9$ months

Average salary = Average salary for 10 months preceding the date of retirement is to be considered

Meaning of salary = Basic salary + DA (forming part of salary) + % commission on turnover

Average Salary = $(27,000 \times 4 + 30,600 \times 6) / 10 = ₹29,160$ per month.

Limit = $9 \times 29,160 = ₹2,62,440$

Rule 2: $10 \times$ Average monthly salary = ₹2,91,600

Rule 3: ₹3,00,000

Rule 4: Actual leave encashment = ₹4,05,000

Exemption = ₹2,62440

Taxable amount = leave encashment received – exemption = ₹1,42,560

(4) Taxable Pension:

Uncommuted pension (fully taxable): $18,000 \times 2 + 9,000 \times 1 = ₹45,000$

Commuted pension: Exempt upto $1/3^{\text{rd}}$ of full value of pension as per section 10 (as employee is receiving gratuity)

Full value of pension = commuted pension/percentage commuted $\times 100$

= $6,30,000 / 50 \times 100 = ₹12,60,000$

Exemption = $12,60,000 / 3 = ₹4,20,000$

Taxable commuted pension = actual pension – exemption = $6,30,000 - 4,20,000 = ₹2,10,000$

(5) Lump sum receipt from URPF at the time of retirement:

Balance of:

Employer's contribution (Taxable as salary): ₹2,76,750

Employee's contribution (not taxable): ₹2,76,750

Interest on employer's contribution (Taxable as salary): ₹1,50,300

Interest on employees' contribution (Taxable as income from other sources): ₹1,50,300.

Important Note: Please refer Tax Laws and Practice, Executive Programme study material for details of the provisions relating to Income under the head salaries.

INCOME FROM HOUSE PROPERTY (SECTION 22 TO 27)

BASIS OF CHARGE

The annual value of property consisting of any building or land appurtenant thereto of which the assessee is the owner, other than such portions of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to income-tax, shall be chargeable to income-tax under the head "Income from house property".

Conditions for income to be taxable as Income from House Property

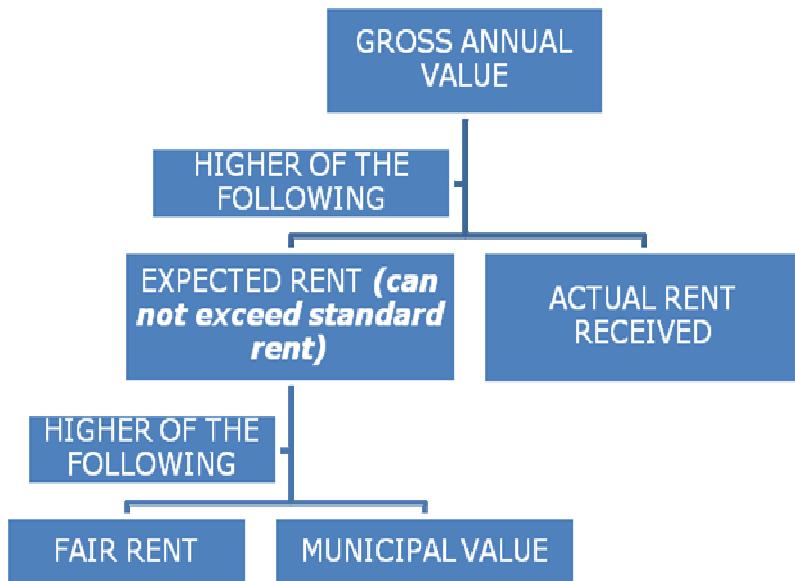
1. There must be a Building or land appurtenant thereto
2. Assessee must be the owner of House Property
3. Assessee should not use the House Property for his own business or profession

If the above conditions are satisfied than the annual value of the house property shall be taxable. For this, the concept of annual value need to be understood. Before moving to the basic concepts let's see how the income from house property is calculated.

Particulars	Let Out (Deemed Let Out Property)	Self Occupied for Residence	Vacant
Gross Annual Value (GAV)	xxx	Nil	Nil
Less: Municipal Taxes paid by owner during the relevant previous year	(xxx)	Nil	(xxx)
Net Annual Value (NAV)	xxx	Nil	(xxx)
Less: Deductions u/s 24			
– Standard Deduction @ 30% of Net Annual Value	(xxx)	–	–
– Interest on borrowed capital	(xxx)	(xxx)*	(xxx)
Income (Loss) from House Property	xxx	(xxx)	(xxx)
Add: Arrears of rent, if not taxed earlier (Receipt – 30% deduction)	xxx	xxx	xxx
Add: Recovery of unrealised rent	xxx	xxx	xxx
Income (loss) from House Property (total)	xxx	xxx	xxx

* Restricted to ₹30,000/₹1,50,000 as the case may be.

GROSS ANNUAL VALUE (GAV)



GAV is higher of Expected Rent or Actual Rent

Less: Unrealised rent of relevant PY

Note: GAV will be Actual Rent if Actual rent is lower than expected rent because of vacancy.

(i) **Expected Rent** is higher of Fair Rent or Municipal Valuation but subject to Standard Rent.

If fair rent is not given, actual rent per month will be considered as fair rent.

(ii) **Actual Rent** is rent for let out period

SELF OCCUPIED FOR RESIDENCE/DEEMED LET OUT PROPERTY

If more than one house property is used for residence, then only one house property at the option of the assessee to be treated as Self Occupied Property and other house property/properties shall be treated as deemed to be let out property.

INTEREST ON BORROWED CAPITAL

1. Interest on borrowed capital shall be allowed as deduction on due basis if loan is taken for Purchase, Construction, Repairs, Renewal, Reconstruction, Renovation and Repayment of existing loan.

2. **Interest in case of Self occupied property:** Actual amount of interest or ₹ 1,50,000 whichever is lower (if loan is taken for purchase or construction on/after 1.4.1999 and purchase and construction completed within 3 years from the end of FY in which loan was taken) is allowed as deduction. Otherwise, actual amount of interest or ₹ 30,000 whichever is lower, is allowed as deduction.

3. **Post construction period interest:** Interest due for the relevant previous year.

4. **Pre construction period interest:** Interest for the period beginning from date of borrowing to earlier of the following two dates:

- 31st March immediately preceding the purchase or construction or

- Date of complete repayment of loan

It is allowed in 5 equal annual instalments starting from the year in which purchase or construction takes place.

5. **Interest payable outside India:** It is not allowed as deduction if tax is not deducted or deposited on the same.

CO-OWNERSHIP OF A HOUSE PROPERTY

If property self-occupied for residence and portion of each co-owner is certain: Treat each part as separate HP and Deduction upto ₹30,000/₹1,50,000 is available to each co-owner.

If used otherwise (i.e. let out): Compute total income from HP and then divide according to proportions owned.

COMPOSITE RENT

If rent is separable into rent from building and rent from other facilities: Rent from the building is to be taxable as Income from House Property. Rent from other facilities/service to be taxable as Income from other sources/Profits and gains of business or profession, as the case may be.

If rent is inseparable: Entire amount of rent is to be taxable as Income from other sources or Profits and gains of business or profession, as the case may be.

DEEMED OWNERSHIP [SECTION 27]

Transferor/any other person will be deemed to be owner in the following cases and not the legal owner:

- (a) **Transfer to Spouse for inadequate consideration:** Transferor will be treated as deemed owner. However, transferor will not be treated as owner if property is transferred to spouse in pursuance of an agreement to live apart.
- (b) **Minor Child:** Parent will be treated as deemed owner. However, in case of transfer to minor married daughter, parent will not be treated as deemed owner.
- (c) **Co-operative Society or Company:** In case house property is in the name of co-operative society or company but the beneficial owner is member or shareholder of these, then deemed owner will be member/shareholder of such co-operative society or company.
- (d) **Part performance of contract:** In case possession of immovable property has been transferred in part performance of the contract, then deemed owner would be the person having possession.
- (e) **Lease of atleast 12 years:** In case immovable property is on lease and lease period exceeds 12 years and at least one year at a time renewable thereafter, then, lessee will be deemed as owner in this case.

Illustration

A has three house properties situated at Delhi.

Property I is let out for residence. Property II is let out for commercial purposes. Property III has four identical units: Unit A (let out for residential purposes throughout PY), Unit B (used for own business), Unit C (used for own residence) and Unit D (Let out for residential purposes; but w.e.f. 1.1.2014 was also used for own residence).

The particulars of property I and II are as under:

Particulars	I (₹)	II (₹)
<i>Municipal Value</i>	<i>50,000</i>	<i>60,000</i>
<i>Actual Rent</i>	<i>5000 pm</i>	<i>6000 pm</i>
<i>Fair rent</i>	<i>70000</i>	<i>75000</i>
<i>Standard Rent</i>	<i>54000</i>	<i>84000</i>
<i>Date of completion of construction</i>	<i>1.3.2005</i>	<i>1.3.1992</i>
<i>Municipal tax paid</i>	<i>10,000</i>	<i>20,000</i>
<i>Repairs</i>	<i>5000</i>	<i>-</i>
<i>Collection charges</i>	<i>4800</i>	<i>4800</i>
<i>Insurance premium paid</i>	<i>2000</i>	<i>2000</i>
<i>Interest on money borrowed for construction</i>	<i>30000</i>	<i>11000</i>

A had borrowed a sum of 300000 @ 10% p.a. on 1.1.2006 for construction of House I. The entire loan is still outstanding though interest is being paid every year.

The particulars of Property III are as under:

Date of completion of construction: 1.3.1995; Date of purchase by R: 1.5.1996.

	₹
<i>Municipal Value</i>	160000
– <i>Rent of Unit A</i>	3000 pm
– <i>Rent of Unit D</i>	3000 pm
– <i>Municipal tax paid</i>	20,000
<i>Other expenses:</i>	
– <i>Repair of Unit A</i>	5000
– <i>Repair of Unit B</i>	10000
– <i>Collection charges of Unit A</i>	3000
– <i>Collection charges of Unit D</i>	2400
– <i>Insurance premium of house property</i>	3000
– <i>Interest on money borrowed for purchase of house</i>	40000
– <i>Lease rent of land of house property</i>	5000

Compute the income of A under the head Income from HP for the AY 2014-15.

Solution

Computation of Income from House Property of Mr. A for the Assessment Year 2014-15 (Previous year 2013-14)

Particulars	I	II	(Amount in ₹)		
			A	III	D
C					
Computation of Gross Annual Value (GAV)				Not required	
Fair Rent (a)	70,000	75,000	36,000		36,000
Municipal valuation (b)	50,000	60,000	40,000		40,000
Standard Rent (c)	54,000	84,000	N.A.		N.A.
Expected Rent: Higher of (a) or (b) but subject to (c)	54,000	75,000	40,000		40,000
Actual rent: Rent for let out period	60,000	72,000	36,000		27,000
GAV = Higher of expected or actual rent minus unrealised rent of previous year	<u>60,000</u>	<u>75,000</u>	<u>40,000</u>		<u>40,000</u>
Computation of Income (loss) from house property:					
GAV	60,000	75,000	40,000	Nil	40,000
Less: Municipal taxes paid by owner during relevant previous year	<u>(10,000)</u>	<u>(20,000)</u>	<u>(5,000)</u>	<u>Nil</u>	<u>(5,000)</u>
Net Annual Value (NAV)	50,000	55,000	35,000	Nil	35,000
Less: Deductions under section 24					
– Standard Deduction @ 30% of NAV	<u>(15,000)</u>	<u>(16,500)</u>	<u>(10,500)</u>	<u>Nil</u>	<u>(10,500)</u>
– Interest on borrowed capital	<u>(30,000)</u>	<u>(11,000)</u>	<u>(10,000)</u>	<u>(10,000)</u>	<u>(10,000)</u>
Income (loss) from house property	<u>5,000</u>	<u>27,500</u>	<u>14,500</u>	<u>(10,000)</u>	<u>14,500</u>

Total Income from house property = ₹ 51,500

Note: Unit of House III will be assessed under the head "Profits and gains of business or profession".

Illustration

Calculate the taxable Income of A for the Assessment Year 2014-15:

A owns a residential flat in Delhi, details of which are given below:

	₹
Municipal value p.a.	1,66,000
Fair rent p.a.	1,18,000
Standard rent p.a.	1,85,000
Expenses incurred by A:	
– Municipal taxes (actually paid)	7,000
– Repairs	1,100
– Common maintenance charges	5,000
– Insurance	2,500
– Interest on capital borrowed for acquiring the flat (Date of borrowing: 10.6.1994)	84,000

The flat is let out upto 31.1.2014 on a monthly rent of ₹20,000 per month. From 1.2.2014, the flat is self occupied for own residence.

The income of A from other sources is ₹1,25,000.

Solution

Computation of taxable income of A for AY 2014-15 (PY 2013-14)

Particulars	Amount (₹)
Computation of Gross Annual Value (GAV)	
Fair Rent (a)	1,18,000
Municipal valuation (b)	1,66,000
Standard Rent (c)	1,85,000
Expected Rent: Higher of (a) or (b) but subject to (c)	1,66,000
Actual rent: rent for let out period	<u>2,00,000</u>
GAV = Higher of expected or actual rent minus unrealised rent of previous year	2,00,000
Computation of Income (loss) from house property:	
GAV	2,00,000
Less: Municipal taxes paid by owner during relevant previous year	<u>(7,000)</u>
Net Annual Value (NAV)	<u>1,93,000</u>
Less: Deductions under section 24	
Standard Deduction @ 30% of NAV	(57,900)
Interest on borrowed capital	<u>(84,000)</u>
Income (loss) from house property	51,100
Income from other sources	<u>1,25,000</u>
Gross Total Income (GTI)	1,76,100
Less: Deductions	<u>Nil</u>
Taxable Income (Total Income)	1,76,100

Illustration

A owns two houses and both are used by him for his own residence. He intends to treat one such house as self occupied and the other as deemed to be let out. Your advice is sought as to the beneficial option based on the following information for the assessment year 2014-15:

Particulars	House I (₹)	House II (₹)
Fair rent (rent which similar property will fetch)	72,000	68,000
Municipal valuation	84,000	52,000
Standard rent	90,000	60,000
Municipal taxes levied	20,000	14,000
Municipal taxes paid	10,000	7,000
Repairs	14,000	12,000
Insurance premium	3,000	2,200
Interest on loans (borrowed during August, 2006 for repairs)	62,000	18,000

Solution

Advice as to which house should be treated as self occupied for residence will depend upon computation of Income from house property. That house will be opted which minimizes the Income or maximizes the loss from house property. Three steps need to be followed for computation:

Step 1: Calculate income from house property assuming both the self occupied houses as deemed to be let out.

Step 2: Calculate income from house property assuming both the houses will be self occupied for residence.

Particulars	Step 1 (Both houses deemed to be let out)		Step II (Both houses self occupied for residence)	
	I	II	I	II
Computation of Gross Annual Value (GAV)				
Fair Rent (a)	72,000	68,000	–	–
Municipal valuation (b)	84,000	52,000	–	–
Standard Rent (c)	90,000	60,000	–	–
Expected Rent: Higher of (a) or (b) but subject to (c)	84,000	60,000	–	–
Actual rent: rent for let out period	Nil	Nil	–	–
GAV = Higher of expected or actual rent minus unrealised rent of previous year	84,000	60,000	–	–
Computation of Income (loss) from house property:				
GAV	84,000	60,000	–	–
Less: Municipal taxes paid by owner during relevant previous year	(10,000)	(7,000)	–	–
Net Annual Value (NAV)				
	74,000	53,000	Nil	Nil
Less: Deductions under section 24				
- Standard Deduction @ 30% of NAV	(22,200)	(15,900)	Nil	Nil
- Interest on borrowed capital	(62,000)	(18,000)	(30,000)*	(18,000)*
Income (loss) from house property				
	(10,200)	19,100	(30,000)	(18,000)

*Interest in case of self occupied house is restricted to lower of actual interest or ₹ 30,000.

Step 3: Make Options for calculating Income from house property:

Option 1: House I as self occupied and House II as deemed to be let out

Income (loss) from house property = $(30,000) + 19,100 = (10,900)$

Option 2: House II as self occupied and House I as deemed to be let out.

Income (loss) from house property = $(18,000) + (10,200) = (28,200)$

Advice: 2nd Option should be chosen (as it maximizes the loss) i.e. House II should be treated as self occupied for residence and House I as deemed to be let out. By doing so, loss from house property would be ₹ 28,200.

Note: For details, please refer the Tax Laws and Practice Executive Programme Study Material.

PROFITS AND GAINS OF BUSINESS OR PROFESSION (SECTION 28 TO 44DB)

1. CHARGING SECTION [SECTION 28]

Following incomes are taxable under the head profits and gains of business or profession:

- (a) The profits and gains of any business or profession carried on by the assessee at any time during the relevant previous year;
- (b) Profits on sale of a licence granted under the Imports (Control) Order, 1955;
- (c) Cash assistance received or receivable by any person against exports under any scheme of the Government of India;
- (d) Any duty of customs or excise repaid or repayable as drawback to any person against exports;
- (e) The value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession;
- (f) Any interest, salary, bonus, commission or remuneration, by whatever name called, due to, or received by a partner of a firm from such firm;
- (g) Any sum, whether received or receivable in cash or kind,
 - (i) Under an agreement for not carrying out any activity in relation to any business; or
 - (ii) Not sharing any know-how, patent, copyright, trademark, licence, franchise or any other business or commercial rights of similar nature or information or technique likely to assist in the manufacture or processing of goods or provision for services.
- (h) Any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy.
 - (i) Income from speculative transaction.

Notes:

- (i) As per Section 2(13) of the Act, business includes trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.
- (ii) As per section 2(36) of the Act, Profession includes vocation.

2. COMPUTATION OF BUSINESS INCOME [SECTION 29]

Business income shall be computed in accordance with the provisions of section 30 to 43D of the Act.

Following format may be used for computing the income under the head “Profits and gains of business or profession”:

Particulars	Amount (₹)
Profit as per Profit and Loss Account	XXX
Add: Inadmissible (Disallowed) expenses if debited to Profit and Loss Account	XXX
Less: Admissible expenses if not debited to Profit and Loss Account	(XXX)
Less: Incomes taxable under any other head or exempt incomes or incomes not taxable, if credited to Profit and Loss Account	(XXX)
Add: Incomes taxable as business or professional income, if not credited to Profit and Loss Account	<u>XXX</u>
TOTAL	XXX
Add: Depreciation as per Profit and Loss Account	XXX
Less: Depreciation as per Income-tax Act	<u>(XXX)</u>
Income under the head “Profits and Gains of Business or Profession”	<u>XXX</u>

3. METHOD OF ACCOUNTING [SECTION 145]

Income from business or profession is computed as per the method of accounting followed by the assessee.

Assessee has the choice of following either the accrual/mercantile method or cash basis of accounting.

If the assessee maintains its accounts on mercantile basis, the income would be taxable on accrual basis irrespective of receipt. A company is required to maintain its accounts only on mercantile system.

However, if the accounts are maintained on the cash basis, then, income would be chargeable to tax in that financial year in which it is received irrespective of accrual.

Note: In this chapter, the word ‘paid’ means actually paid or payable as per the method of accounting followed by the assessee.

4. DEDUCTION IN RESPECT OF EXPENDITURE ON REPAIRS ETC. OF BUILDING [SECTION 30]

The following deductions are allowed in respect of premises used for the business or profession:

- Any sum on account of land revenue, local taxes or municipal taxes subject to provisions of section 43B of the Act i.e. these will be allowed in the relevant previous year only when actually paid upto due date of return of Income, otherwise, these will be allowed in the year of payment.
- Lease rent of the premises, if premises is taken on rent/hire/lease by the assessee. Owner can claim depreciation on premises.
- Insurance charges against the risk of damage or destruction of building are allowed as deduction;
- Current repairs are allowed to tenant or owner, whosoever bear the cost of repairs for its business or profession;
- Capital repairs incurred by the assessee are not allowed as deduction whether premises is occupied as a tenant or as an owner. However, the assessee can claim depreciation on capital repairs.

As per Section 32, any capital expenditure incurred by the assessee for the purpose of the business or profession in a building not owned by him then, such capital expenditure incurred shall be treated as deemed building for which the assessee (tenant) can claim depreciation.

Note: As per Section 38 of the Act, where the building, plant, machinery or furniture is not used exclusively for the purpose of business or profession, then the deduction of expenses incurred shall be restricted to a fair proportion of above expenditure which the assessing officer may determine.

5. DEDUCTION IN RESPECT OF EXPENDITURE ON PLANT, MACHINERY OR FURNITURE [SECTION 31]

Current repairs to the plant, machinery and furniture is allowed as deduction. Capital repairs are never allowed as deduction whether plant is leased or purchased. Depreciation on such capital expenditure may be claimed.

Insurance premium paid for insurance against the risk of damage or destruction of plant, machinery or furniture is allowed as deduction.

6. DEPRECIATION [SECTION 32]

Depreciation is allowed as deduction under section 32 of the Act if the asset is owned (wholly or partly) by the assessee and such asset is put to use during the relevant previous year for the purpose of business or profession.

Depreciation is charged from the day when the asset is put to use (and not the actual use) and not from the day of its acquisition. Use of the asset may be active or passive for claiming depreciation. Therefore, even on standby equipments kept ready for replacement/use, depreciation will be allowed although these might not be used in the previous year.

Depreciation under the Income-tax Act is allowed on the basis of block of assets as per written down value (WDV) method of calculating depreciation.

However, units engaged in the power sector can claim depreciation either on straight line method (individually on each asset) or on written down value method on block of asset. The option of charging depreciation either on straight line method or written down value method should be exercised before the due date of furnishing of return. However, once the option is exercised it shall be final and shall apply to all the subsequent assessment years.

Block of Assets [Section 2(11)]

It means a group of assets falling within a class of assets in respect of which same rate of depreciation is prescribed.

There are four classes of assets on which depreciation is allowed i.e. Building, Furniture or fittings, Plant & Machinery and Intangible assets. Separate rates of depreciation are prescribed for these asset classes.

Therefore, example of a block of asset may be two buildings (same class) having depreciation rate of 10% (same rate) (this will constitute one block of asset for calculating depreciation) and another block could be three machines(same class) having depreciation rate of 15% (same rate).

Depreciation rates

➤ **Buildings:** General rate of depreciation on building is 10%. However, residential building used by employees is allowed depreciation @ 5%.

Further, building which are used as temporary structures are allowed depreciation @ 100%.

➤ **Furniture or fittings including electrical fittings:** There is only one rate in case of furniture and fittings, i.e. 10%.

➤ **Plant and Machinery:** General rate of depreciation on Plant and machinery is 15%. However, there are certain special rates as follows:

- Motor Cars : 15%;
- Computers including computer software : 60%;
- Books not being annual publication, and owned by professional : 60%;
- Books (being annual publication) owned by assessee carrying on a profession : 100%;
- Books owned by an assessee carrying on business in running lending libraries : 100%;
- Pollution control equipments : 100%; Ships : 20%;
- Aeroplanes or Aeroengines : 40%.

➤ **Plant:** As per Section 43(5), plant includes ships, vehicles, books, scientific apparatus and surgical equipment used for the purpose of the business or profession. It does not include tea bushes or livestock or buildings or furniture and fittings.

➤ **Intangible Assets (Know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets acquired after 31.3.1999):** Depreciation is allowed @ 25% on these assets.

Depreciation at Half rate: When the asset is purchased and put to use in the same previous year for less than 180 days then half rate of depreciation is applicable. Otherwise, depreciation at full rate is applicable.

Additional depreciation

It is available to an assessee engaged in the business of manufacture or production of an article or thing as well as assessee engaged in the business of generation or generation and distribution of power. It is allowed on any new Plant and Machinery (not on second hand machinery whether used in India or outside India). However, it is not allowed on buildings and furniture, road transport vehicles, ships and aircraft, any office appliances, any machinery or plant installed in any office premises or any residential accommodation, or guest house. It is also not allowed on plant and machinery the full cost of which is allowed as deduction under any provision.

Additional depreciation is over and above normal depreciation and is allowed @ 20%. However, if the asset is acquired and put to use in the same previous year for less than 180 days then rate of additional depreciation is 10%. It is computed on the individual assets and is allowed only for first year of acquisition of the asset.

Computation of depreciation for a block of assets

Particulars	Amount (₹)
Written down value (WDV) of block as on 1 st day of relevant Previous year (1.4.2013 for AY 2014-15)	XXX
Add: Acquisitions of assets in the block during the relevant previous year:	
– Assets acquired and put to use for 180 days or more in the PY	XXX
– Assets acquired and put to use for less than 180 days	XXX
Less: Moneys payable (receivable) in respect of any buildings, machinery, plant or furniture on disposal of assets	(XXX)
WDV before depreciation	XXX
Less: Depreciation for the relevant previous year (PY 2013-14)	
– Depreciation @ half rate on assets acquired and put to use for less than 180 days during relevant PY;	(XXX)
– Depreciation @ full rate on other assets	(XXX)

Less: Additional depreciation, if any, allowed to assessee during the PY:

- Depreciation @ 10% on eligible assets acquired and put to use for less than 180 days during relevant PY; (XXX)
- Depreciation @ 20% on other assets (XXX)

WDV of the block as on 1.4.2014

XXX

Note:

- (a) **Actual cost [Section 43(1)]:** Actual cost means the actual cost of the assets to the assessee, reduced by that portion of the cost thereof, if any, as has been met directly or indirectly by any other person or authority. As per an explanation to section 43(1), interest pertaining to the period till the asset is put to use shall be treated as part of the actual cost of the asset.

Explanations to Section 43(1):

1. Cost of the asset used subsequent to Scientific research shall be nil.
2. **Actual cost in case of asset acquired by way of gift or inheritance:** It will be actual cost to the previous owner minus depreciation actually allowed/allowable as if the asset was the only asset in that block;
3. **Actual cost if the asset is used by the previous owner:** Where, before the date of acquisition of the asset, the asset was used by any other person at any time for his business and the AO is satisfied that the main purpose of transfer of asset is to reduce the tax liability by claiming depreciation on higher cost, actual cost in such a case will be the amount determined by the AO, with the previous approval of the Joint Commissioner, having regard to all the circumstances of the case.
4. **Re-acquired asset:** Actual cost in this case will be lower of original cost price or re-acquired price.
5. **Building brought into use for business:** Actual cost shall be the cost after allowing depreciation as if the building since acquisition was used for business.
6. **Assets transferred by holding company to 100% subsidiary or vice-versa where transferee is an Indian company:** Actual cost shall be the same as if the transferor company had continued to hold the capital asset for the purpose of its business.
7. **Assets transferred under a scheme of amalgamation:** Actual cost shall be the same as if the transferor company had continued to hold the capital asset for the purpose of its business.
8. **Asset transferred to the resulting company in the case of demerger:** Actual cost shall be the same as if the transferor company had continued to hold the capital asset for the purpose of its business.
9. **Refund of duty:** Refund of duty will be reduced while calculating actual cost.
10. Cost borne by other agencies (subsidies) shall be reduced while calculating actual cost.
11. Actual cost of an asset brought to India by a non resident shall be the cost after allowing depreciation as if the asset was used in India since its acquisition.
12. Actual cost in the case of corporatisation of a recognised stock exchange in India shall be the same as if the transferor company had continued to hold the capital asset for the purposes of its business.
13. Actual cost of asset used in business after use for specified business under section 35AD: Actual cost of the asset will be Nil.

- (b) Disposal of assets:** Where any building, machinery, plant or furniture is sold, discarded, demolished or destroyed in the previous year the amount by which the moneys payable in respect of such building, machinery, plant or furniture, together with the amount of scrap value, shall be deducted from the opening WDV.

Moneys payable in respect of any building, machinery, plant or furniture includes any insurance, salvage or compensation moneys payable in respect thereof; and where the building, machinery, plant or furniture is sold, the price for which it is sold (Sold includes a transfer by way of exchange or a compulsory acquisition under any law for the time being in force).

- (c) Capital Gain/Loss in case of depreciable assets [Section 50]:**

Section 50 is applicable only when there is no asset in the block of assets on the last day of the previous year (Short term capital gain/short term capital loss can arise in this case) or where the WDV of the block of the asset on the last day of the previous year is zero (only Short term capital gain will arise in this case, as sale proceeds of the asset/s will exceed the opening WDV and acquisitions during the previous year).

- (d) Depreciation in case of Succession/Amalgamation/Demerger:** The aggregate of depreciation allowable to the predecessor and successor or to the amalgamating and the amalgamated company or to the demerged company and the resulting company shall not exceed in any previous year the depreciation calculated at the prescribed rates as if the succession or amalgamation or demerger, had not taken place.

Such depreciation shall be apportioned between the predecessor and successor, or the amalgamating and amalgamated company or the demerged and resulting company, in the ratio of the number of days for which the assets were used by them.

7. INCENTIVE FOR ACQUISITION AND INSTALLATION OF NEW PLANT OR MACHINERY BY MANUFACTURING COMPANY [SECTION 32AC] (AMENDMENT BY THE FINANCE ACT, 2013)

In order to encourage substantial investment in plant or machinery, a new section 32AC is inserted in the Income-tax Act to provide that where an assessee, being a company,

- (a) is engaged in the business of manufacture of an article or thing; and
- (b) invests a sum of more than ₹ 100 crore in new assets (plant or machinery) during the period beginning from 1st April, 2013 and ending on 31st March, 2015,

then, the assessee shall be allowed

- (i) for assessment year 2014-15, a deduction of 15% of aggregate amount of actual cost of new assets acquired and installed during the financial year 2013-14, if the cost of such assets exceeds ₹100 crore;
- (ii) for assessment year 2015-16, a deduction of 15% of aggregate amount of actual cost of new assets, acquired and installed during the period beginning on 1st April, 2013 and ending on 31st March, 2015, as reduced by the deduction allowed, if any, for assessment year 2014-15.

The phrase "new asset" has been defined as new plant or machinery but does not include:

- (i) any plant or machinery which before its installation by the assessee was used either within or outside India by any other person;

- (ii) any plant or machinery installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house;
- (iii) any office appliances including computers or computer software;
- (iv) any vehicle;
- (v) ship or aircraft; or
- (vi) any plant or machinery, the whole of the actual cost of which is allowed as deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head "Profits and gains of business or profession" of any previous year.

Further, suitable safeguards are provided under the section so as to restrict the transfer of the plant or machinery for a period of 5 years. However, this restriction shall not apply in a case of amalgamation or demerger but shall continue to apply to the amalgamated company or resulting company, as the case may be.

This amendment will take effect from 1st April, 2014 and will, accordingly, apply in relation to the assessment year 2014-15 and subsequent assessment year.

8. TEA, COFFEE AND RUBBER [SECTION 33AB READ WITH RULE 5AC]

An assessee carrying on business of growing and manufacturing tea or coffee or rubber in India, has before the expiry of 6 months from the end of the previous year or before the due date of furnishing the return of his income, whichever is earlier, deposited any amount in National Bank for Agricultural and Rural Development (NABARD) under a Tea, Coffee, Rubber Board scheme, then he shall be allowed a deduction of lower of amount so deposited or a sum equal to 40% of the profits of such business. Accounts should be audited.

9. SITE RESTORATION FUND [SECTION 33ABA READ WITH RULE 5AD]

This deduction will be allowed to an assessee carrying on business of consisting of the prospecting for petroleum or natural gas or extraction or production of petroleum or natural gas or both in India and in relation to which the Central Government has entered into an agreement with such assessee for such business, if it has made specified deposits in the prescribed time period.

Assessee has to deposit any amount before the end of the previous year in State Bank of India under Ministry of Petroleum and Natural Gas Scheme or any other nationalised bank, to claim such deduction.

Deduction shall be lower of (a) amount deposited or (b) 20% of profits of such business. The accounts of the assessee should be audited.

10. EXPENDITURE ON SCIENTIFIC RESEARCH [SECTION 35]

Scientific research means any activity for the extension of knowledge in the fields of natural or applied sciences including agriculture, animal husbandry, fisheries.

Revenue expenditure on In-house scientific research [Section 35]

Any revenue expenditure (certified by prescribed authority) laid out or expended on scientific research related to the business carried on by the assessee is allowed as deduction.

Where any revenue expenditure is incurred before the commencement of business on payment of salary (other than value of perquisite) to an employee engaged in such scientific research or on the purchase of

materials used in scientific research, the aggregate of such expenditure incurred within 3 years immediately preceding the commencement of business is allowed in the PY in which business is commenced.

Capital expenditure on in-house scientific research

Any capital expenditure (other than on land or its development) laid out or expended on scientific research related to the business carried on by the assessee is allowed as deduction.

Where any capital expenditure is incurred before the commencement of business, the aggregate of such expenditure incurred within 3 years immediately preceding the commencement of business is allowed in the PY in which business is commenced.

Higher (double) deduction for expenditure (revenue or capital) on In-house scientific research in certain cases

If a company is engaged in the business of manufacture or production of any article or thing other than those specified in the Eleventh schedule (i.e. other than alcohol, tobacco, cosmetics, tooth pastes, cold drinks, chocolates, steel almirah, safes, cork, rubber, office machines) and it incurs any expenditure, revenue or capital (other than on land and building), then deduction of 2 times of expenditure will be allowed to such company provided following conditions are satisfied:

- The taxpayer has entered into an agreement with the prescribed authority for co-operation in such research and development and for audit of accounts maintained for that facility.
- Such Research and development facility is approved by the prescribed authority.

Contribution for Scientific Research:

Contribution to outsiders for research is fully allowed as deduction whether research is related or unrelated to the business of the assessee.

Deduction for an amount equal to two times of contribution to following agencies is allowed as deduction:

- Approved research association including social and statistical research;
- Approved university, colleges or other institution engaged in scientific research;
- Indian company having main object as scientific research being approved by prescribed authority;
- National Laboratory;
- Indian Institute of Technology (IITs)

The higher deduction of 200% is allowed if above payment is made under a specific direction that the said sum shall be used for scientific research undertaken under a programme approved in this behalf by the prescribed authority.

Otherwise, deduction @ 175% of the expenditure is allowed if contribution made to the specified agencies mentioned above.

The deduction is allowed even if after the date of making the contributions, the approval granted to the institution/s has been withdrawn.

11. TELECOMMUNICATION LICENCE [SECTION 35ABB]

Where capital expenditure is incurred for acquiring telecommunication licence, then deduction is allowed for such expenditure over the period of licence or if licence has been obtained before commencement of business, then deduction will be allowed for the unexpired period of licence.

Deduction = Licence fees paid/Unexpired period of licence from the date of payment.

12. ELIGIBLE PROJECTS OR SCHEMES [SECTION 35AC]

Assessee shall be allowed a deduction of the amount of expenditure paid to a public sector company or a local authority or to an association or institution approved by the National Committee for carrying out any eligible project or scheme or for the payment made to a corporate assessee who itself carries out any eligible project or scheme.

Eligible project or scheme means such project or scheme for promoting the social and economic welfare of, or the uplift of, the public.

13. DEDUCTION IN RESPECT OF EXPENDITURE ON SPECIFIED BUSINESS [SECTION 35AD]

The whole of expenditure of capital nature (other than on acquisition of land or goodwill or financial instrument) incurred, wholly and exclusively, for the purpose of any specified business carried on by the assessee is eligible for deduction.

The deduction shall be available during the previous year in which such expenditure is incurred. However, if the expenditure is incurred prior to commencement of its operations, the deduction shall be available in the previous year in which the operations of the specified business are commenced provided the amount is capitalised in the books of accounts of the assessee on the date of commencement of its operations.

Specified businesses

- (a) Setting up and Operating a cold chain facility;
- (b) Setting up and operating a warehousing facility for storage of agricultural produce;
- (c) Laying and operating a cross-country natural gas or crude or petroleum oil pipeline network for distribution, including storage facilities being an integral part of such network;
- (d) Building and operating a new atleast 2 star hotel anywhere in India;
- (e) Building and operating a new atleast 100 bed patients hospital anywhere in India;
- (f) Developing and building a housing project in a scheme for slum redevelopment or rehabilitation;
- (g) Developing and building a housing project in a scheme for affordable housing framed by Government and notified by CBDT.
- (h) New plant or newly installed capacity in an existing plant for production of fertilizers.
- (i) Setting up and operating an Inland Container depot or a Container freight station notified or approved under the Customs Act, 1962.
- (j) Bee keeping and production of honey and beeware.
- (k) Setting up and operating a warehousing facility for storage of sugar.

Note:

If any asset on which deduction is allowed u/s 35AD is transferred or destroyed, then any amount recoverable is chargeable as business income.

Deduction of afore-mentioned shall be allowed only from such income and other specified business income and shall be carried forward for unlimited period as per Section 73A.

Where the specified business is of the nature referred to in (i), (j), or (k) and has commenced its operations on or after 1st day of April, 2012, the deduction under Sub-section (1) of Section 35AD shall be allowed of an amount equal to one and one half times (150%) of the expenditure referred above.

14. RURAL DEVELOPMENT PROGRAMMES [SECTION 35CCA]

The assessee shall be allowed a deduction of the amount of payment to an association or institution, which has as its object the undertaking of any programme of rural development or payment to an association or institution which has as its object the training of persons for implementing programmes of rural development or to a rural development fund set up and notified by the Central Government in this behalf or payment to the National Urban Poverty Eradication Fund set up by Central Government.

15. Weighted deduction in respect of expenditure incurred on notified agricultural extension project [Section 35CCC]

With effect from assessment year 2013-14, new section 35CCC has been inserted to provide a weighted deduction of a sum equal to 150% of expenditure incurred by an assessee on agricultural extension project in accordance with the prescribed guidelines. Only those agricultural extension project which are notified by the board shall be eligible for this weighted deduction.

16. Weighted deduction in respect of expenditure incurred by companies on notified skill development project [Section 35CCD]

In order to encourage companies to invest on skill development projects in the manufacturing sector, with effect from assessment year 2013-14, a new section 35CCD has been inserted to provide for a weighted deduction of a sum equal to 150% of the expenditure (not being expenditure in the nature of cost of any land or building) on skill development project incurred by the company in accordance with the prescribed guidelines.

The skill development project eligible for this weighted deduction shall be notified by the Board.

17. PRELIMINARY EXPENSES [SECTION 35D]

Preliminary expenses are specified expenses incurred before setting up of the business or the expenses are incurred in connection with extension of an undertaking or in connection with setting up of a new unit.

Specified preliminary expenses are:

- (a) Preparation of feasibility report;
- (b) Conducting market survey or any other survey necessary for the business;
- (c) Preparation of Project report;
- (d) Engineering services relating to the business;
- (e) Legal charges for drafting an agreement relating to the setting up or conduct of the business;
- (f) Legal charges for drafting and printing of Memorandum of Association (MOA) and Articles of Association (AOA);
- (g) Registration fees of a company paid to Registrar of Companies;
- (h) Expenses and legal charges incurred in drafting, printing and advertising for prospectus;
- (i) Expenditure incurred on issue of shares or debentures like underwriting commission, brokerage.

Deduction for preliminary expenses is allowed to an Indian company or a resident non-corporate assessee in 5 equal annual instalments over a period of 5 years beginning with the previous year in which the business commences or the previous year in which the extension of the undertaking is completed or the new unit commences production or operation.

Amount of Deduction:

In case of non-corporate assessee: Lower of eligible expenditure on scientific research or 5% of cost of project is allowed as deduction.

In case of company assessee: Deduction of eligible expenditure will be limited to higher of 5% of cost of the project or 5% of the capital employed

Cost of project includes cost of the fixed assets, being land, buildings, leaseholds, plant, machinery, furniture, fittings and railway sidings (including expenditure on development of land and buildings).

Capital employed is the aggregate of issued share capital, debenture and long term borrowings.

18. VOLUNTARY RETIREMENT SCHEME EXPENDITURE [SECTION 35DDA]

Where an assessee incurs any expenditure in any previous year by way of payment of any sum to an employee in connection with his voluntary retirement, in accordance with any scheme of voluntary retirement, then deduction for such expenditure will be allowed in 5 equal annual instalments starting from the previous year in which payment is made.

19. PROSPECTING FOR CERTAIN MINERALS [SECTION 35E READ WITH RULE 6AB]

Assessee (being an Indian company or a resident non-corporate assessee) engaged in prospecting, extraction or production of mineral is allowed a deduction of lower of the 1/10th of the amount of such expenditure or profit from mining as computed before making the deduction under this section.

20. DEDUCTIONS UNDER SECTION 36

Following expenses are allowed as deduction while computing income from business or profession:

- (a) **Insurance of stock [Section 36(1)(i)]:** Insurance premium paid in respect of insurance against risk of damage or destruction of stocks or stores used for purpose of business is allowed as deduction;
 - (b) **Insurance premium for life of cattles [Section 36(1)(ia)]:** Premium paid by a federal milk co-operative society insuring the life of the cattle owned by a member of a primary co-operative society, engaged in supplying milk raised by its members to such federal milk co-operative society.
 - (c) **Insurance premium on health of employees [Section 36(1)(ib)]:** Any premium paid by employer on health of employees by modes other than cash, is allowed as deduction. Premium should be paid under a scheme framed in this behalf by the General Insurance Corporation of India and approved by the Central Government or any other insurer and approved by IRDA.
 - (d) **Bonus or commission paid to employees [Section 36(1)(ii)]:** Any sum paid to an employee as bonus or commission for services rendered, is allowed as deduction subject to section 43B of the Act.
 - (e) **Interest paid on money borrowed for the purpose of business or profession [Section 36(1)(iii)]:** Interest paid in respect of capital borrowed for the purpose of business or profession shall be allowed as deduction subject to Section 43B if loan is borrowed from banks or financial institution.
- Interest before commencement of business is not allowed as deduction. However, it can be amortised over a period of 5 years under Section 35D from the Financial year in which business is commenced.
- (f) **Employer's contribution towards Recognised provident fund or an approved superannuation fund [Section 36(1)(iv)]:** It is allowed as deduction subject to section 43B. As per section 40A(9), contribution towards any non-statutory fund or unapproved fund is not allowed as deduction.

- (g) **Employer's contribution towards pension scheme referred in section 80CCD [Section 36(1)(iva)]:** It will be allowed as deduction to the extent of 10% of salary of the employee in the previous year, subject to section 43B.

Salary includes Basic salary and Dearness allowance (forming part of salary for superannuation benefits), but it excludes all other allowances and perquisites.

- (h) **Employer's contribution towards an approved gratuity fund [Section 36(1)(v)]:** It is allowed as deduction subject to section 43B of the Act. As per section 40A(7), contribution towards unapproved gratuity fund is not allowed as deduction. Where employee retires during the year, gratuity actually paid to employee is allowed as deduction if no deduction was claimed earlier.

- (i) **Employee's contribution towards provident funds etc. [Section 36(1)(va)]:** Any sum received by the assessee from his employees as contributions to any provident fund or superannuation fund or any fund set up under the provisions of the Employees' State Insurance Act, or any other fund for the welfare of such employees, is treated as income in the hands of the assessee as per section 2(24) of the Act.

The aforesaid amount is allowed as deduction under section 36(1)(va) only if such employee's contribution is credited in employee's account on or before the 'due date' specified under the specific act relating to provident fund, superannuation fund etc. If this amount is paid after due date, then deduction is never allowed to the assessee.

- (j) **Dead or useless animals [Section 36(1)(vi)]:** In respect of animals which have been used for the purpose of business or profession otherwise than as stock in trade and have died or become permanently useless for such purposes, the differences between the actual cost of the animals and the amount, if any, realised in respect of the carcasses or animals is allowed as deduction.

- (k) **Bad Debts [Section 36(1)(vii)]:** Bad debt should be allowed as deduction if it relates to a debt and such debt should be in respect of a business carried on by the assessee. Such debt has been taken into account in computing the business income of the assessee in any of the earlier previous year.

Deduction of bad debt is allowed if it is written off as irrecoverable in the accounts of the assessee.

- (l) **Special reserve created and maintained by Financial Corporation [Section 36(1)(viii)]:**

Deduction is allowed for special reserve so created by financial corporation to the extent of lower of the following 3 amounts:

- (i) 20% of the profits derived from such business before making deduction under this clause carried to such reserve account, or
- (ii) Amount transferred to special reserve
- (iii) Where such special reserve exceeds from time to time 200% of (paid up share capital and general reserve as on the last day of the previous year minus the balance of the special reserve account on the first day of the previous year), no allowance under this clause shall be made in respect of such excess.

- (m) **Family planning expenditure incurred by Company [Section 36(1)(ix)]:** Revenue expenditure incurred by the company for promoting family planning is fully allowed as deduction.

Capital expenditure for promoting family planning amongst its employees is allowed as deduction in 5 equal annual instalments from the year in which expenditure is incurred.

- (n) **Securities transaction tax (STT) [Section 36(1)(xv)]:** STT paid by the assessee during the previous year shall be allowed as deduction subject to the condition that income from taxable securities transaction is included under the head PGBP.

(o) Commodities Transaction Tax [Introduced by Finance Act, 2013]

A new tax called Commodities Transaction Tax (CTT) is levied on taxable commodities transactions entered into in a recognised association.

Section 36 of the Income-tax Act is amended to provide that an amount equal to the commodities transaction tax paid by the assessee in respect of the taxable commodities transactions entered into in the course of his business during the previous year shall be allowable as deduction, if the income arising from such taxable commodities transactions is included in the income computed under the head "Profits and gains of business or profession".

21. GENERAL DEDUCTION [SECTION 37]

Any expenditure not specifically covered under section 30 to 36 is allowed under section 37 if following conditions are satisfied:

- (a) Expenditure is incurred during the relevant previous year, wholly and exclusively for the purpose of the business;
- (b) Expenditure is not in the nature of personal expenditure; and
- (c) Expenditure is not of capital in nature i.e. expenses should be of revenue in nature.

However, any expenditure incurred which is an offence or which is prohibited by law, shall not be allowed as deduction. Therefore, illegal expenditures like bribes, ransom money will not be allowed as deduction.

Also, expenditure on advertising in any souvenirs, brochure etc. of a political party shall not be allowed as deduction as per section 37(2B).

Notes:

- (a) Donation /Contribution to political party is not allowed as deduction under section 37. However, it is allowed as a deduction under Section 80GGB/80GGC.
 - (b) Annual listing fees is allowed as deduction under section 37. However, initial listing fees is not allowed as deduction.
 - (c) Interest on loan taken for payment of dividend is allowed as deduction as was held to be incurred wholly and exclusively for the purpose of the business. However, interest on loan taken for payment of income tax is not allowed as deduction, being personal in nature.
 - (d) Expenditure on raising loan for the purpose of business is allowed as deduction.
 - (e) Expenditure on raising equity or preference shares is not allowed as deduction as it is in the nature of capital expenditure. However, as per a Supreme Court judgement, expenditure incurred on raising bonus shares is allowed as deduction, being revenue in nature.
 - (f) Payment of direct taxes i.e. income tax and wealth tax is not allowed as deduction under section 37. Corporate dividend tax is also not allowed as deduction.
 - (g) Indirect taxes like excise duty, custom duty, octroi, sales tax, shall be allowed as deduction under section 37 subject to section 43B.
 - (h) Penalty paid for infringement of law is not allowed as deduction e.g. penalty for non-payment of sales tax, excise, custom etc.
- However, penalty paid for not complying with terms and conditions of contract is allowed as deduction since it is breach of contract.
- (i) Business losses are not deductible under section 37 but under section 28 as income includes

losses also. For example:

- (i) Loss on account of robbery, theft, embezzlement etc.
- (ii) Loss on account of valuation of stock in trade;

22. RESTRICTIONS ON DEDUCTIONS (SECTION 40)

(i) Payment to a Non-resident without deduction of tax at source [Section 40(a)(i)]

Any interest, royalty, fees for technical services or other sum chargeable under this Act, which is payable Outside India (to a resident or non-resident) or in India to a non-resident or to a foreign company (resident or non-resident) on which tax is deductible at source and on which such tax has not been deducted or after deduction has not been paid within specified period, is not allowed as deduction while computing business income of an assessee.

Specified period:

- Expenditure relates to the month of April to February: TDS should have been deposited in the same year upto March 31st to claim the deduction in the previous year of expenditure.
- Expenditure relates to month of March: TDS should have been deposited upto the date specified in section 200.

If the amount of TDS is not deposited within the specified period, then deduction of such expenditure is allowed in the year of deposit to Government.

(ii) Payment made to a Resident without tax deduction at source [Section 40(a)(ia)]

Any interest, commission or brokerage, rent, fees for professional services or fees for technical services, royalty or amounts payable to a contractor or sub-contractor, payable to a resident on which tax is deductible at source and on which tax has either not been deducted or after deduction, has not been paid within specified period, is not allowed as deduction while computing business income of an assessee.

Specified period:

- Expenditure relates to the month of April to February: TDS should have been deposited in the same year upto March 31st to claim the deduction in the previous year of expenditure.
- Expenditure relates to month of March: TDS should have been deposited upto the due date of filing return of income by the assessee.

If the amount of TDS is not deposited within the specified period, then deduction of such expenditure is allowed in the year of deposit to Government.

(iii) Payment made by way of Salary [Section 40(a)(iii)]

Any payment chargeable under the head salaries payable outside India (to a resident or to a non-resident) or in India to a non-resident, on which the tax has not been paid thereon nor deducted therefrom, then deduction shall never be allowed.

(iv) Disallowance of certain Fee, Charge, etc. in the case of State Government Undertakings [(Section 40(a)(iib)]

The existing provisions of section 40 specifies the amounts which shall not be deducted in computing the income chargeable under the head "Profits and gains of business or profession". The non-deductible expense under the said section also includes statutory dues like fringe benefit tax, income-tax, wealth-tax, etc.

Disputes have arisen in respect of income-tax assessment of some State Government undertakings as to whether any sum paid by way of privilege fee, license fee, royalty, etc. levied or charged by the State

Government exclusively on its undertakings are deductible or not for the purposes of computation of income of such undertakings. In some cases, orders have been issued to the effect that surplus arising to such undertakings shall vest with the State Government. As a result it has been claimed that such income by way of surplus is not subject to tax. It is a settled law that State Government undertakings are separate legal entities than the State and are liable to income-tax.

In order to protect the tax base of State Government undertakings vis-a-vis exclusive levy of fee, charge, etc. or appropriation of amount by the State Governments from its undertakings, section 40 of the Income-tax Act is amended to provide that any amount paid by way of fee, charge, etc., which is levied exclusively on, or any amount appropriated, directly or indirectly, from a State Government undertaking, by the State Government, shall not be allowed as deduction for the purposes of computation of income of such undertakings under the head "Profits and gains of business or profession". The expression "State Government Undertaking" is also defined for this purpose.

(v) Payment made to Relatives [Section 40A(2)]

Where any payment is made to the relative of any person or person having substantial interest, and the AO is of the opinion that such expenditure is excessive or unreasonable having regard to the fair market value of the goods or services, so much of the expenditure as is so considered by him to be excessive or unreasonable, shall not be allowed as deduction.

However, such excessive and unreasonable amount shall not be disallowed in respect of a specified domestic transaction referred to in Section 92BA, if such transaction is at arm's length price as defined in Clause (ii) of Section 92F.

Note:

(a) Relative [Section 2(41)]: Following persons are treated as relatives:

- **In case of an Individual:** an individual who is relative of the assessee or an individual having a substantial interest in the business of the assessee;
- **In case of a Company:** Director of the company or any relative of a director, An individual having a substantial interest in the business of the assessee;
- **In case of a firm:** Partner of the firm or relative of a partner, An individual having a substantial interest in the business of the assessee;
- **In case of an AOP:** Member of the AOP or relative of a member; An individual having a substantial interest in the business of the assessee;
- **In case of HUF:** Member of the family or relative of such person; An individual having a substantial interest in the business of the assessee.

(b) Meaning of Substantial interest: It means holding of 20% or more share in profits or voting power.

(vi) Cash Expenditure [Section 40A(3)]

Where the assessee incurs any expenditure in respect of which payment or aggregate of payments is made to a person in a single day, of sum exceeding ₹ 20,000 otherwise than by an account payee cheque or an account payee demand draft, for which deduction is claimed, then such expenditure is fully disallowed as a deduction.

Where the payment is made for plying, hiring or leasing goods carriages, the limit of ₹20,000 gets revised to ₹35,000.

Rule 6DD [Exceptions – Where payment in excess of ₹ 20,000/35,000 can be made in cash]:

- (a) Payment made to Financial Institutions or Banks;
- (b) Payment of Sales tax, custom, excise, income tax, etc.;
- (c) Where the payment is made in a village or town, not served by any bank;
- (d) Payment made on a day on which the all banks were closed either on account of holiday or strike;
- (e) Payment made for the purchase of agricultural or forest produce, the produce of animal husbandry (including hides and skins) or dairy or poultry farming, fish or fish products, the products of horticulture or apiculture, to the cultivator, grower or producer of such articles, produce or products;
- (f) Payments made by a book adjustment;
- (g) Where the payment is made for the purchase of the products manufactured or processed without the aid of power in a cottage industry, to the producer of such products.

23. DEEMED INCOME IN CERTAIN CASES [SECTION 41]

- (a) **Cessation of Liability [Section 41(1)]:** Where a deduction has been allowed for any year in respect of a loss, expenditure or trading liability incurred by the assessee and subsequently such amount is cancelled, then it shall be taxable under the head PGBP whether business exists or not.
- (b) **Sale of Scientific Research Asset without being used for any other purpose:** Sale proceeds upto the amount of cost of the asset will be treated as business income and excess if any of sale price over cost will be treated as capital gain.
- (c) **Sale of asset used for promotion of family planning without being used for any other purpose:** Sale proceeds upto the amount of cost of the asset will be treated as business income and excess if any of sale price over cost will be treated as capital gain.

24. BUSINESS FOR PROSPECTING ETC. FOR MINERAL OIL [SECTION 42]

Assessee engaged in the business of prospecting for or extraction or production of mineral oils is allowed the deduction as per the agreement entered with the Central Government.

25. DEDUCTION ON ACTUAL PAYMENT BASIS [SECTION 43B]

In case of specified payments, deduction is allowed on actual payment even if the assessee maintains account on mercantile basis. Deduction is allowed in the relevant previous year if the payment is made for the specified expenditure on or before the due date of return of income. However, if payment is made after due date of return of income, deduction is allowed in the year of actual payment.

Specified expenditures are:

- (a) Any sum payable by the assessee by way of tax, duty, cess or fee, by whatever name called, under any law, i.e. Sales tax, Excise Duty, Custom duty, Municipal taxes, land revenue etc.
- (b) Interest payable on any loan or borrowing from a public financial institution or from a State financial corporation or from a State Industrial Investment Corporation.
- (c) Interest payable on any term loan or advance from a scheduled bank.
- (d) Employer's contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of employees; or
- (e) Any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee.
- (f) Bonus or commission payable to employees.

26. COMPUTATION OF INCOME UNDER THE HEAD "PROFITS AND GAINS OF BUSINESS OR PROFESSION" FOR TRANSFER OF IMMOVABLE PROPERTY IN CERTAIN CASES (SECTION 43CA) (INTRODUCED BY THE FINANCE ACT, 2013)

Currently, when a capital asset, being immovable property, is transferred for a consideration which is less than the value adopted, assessed or assessable by any authority of a State Government for the purpose of payment of stamp duty in respect of such transfer, then such value (stamp duty value) is taken as full value of consideration under section 50C of the Income-tax Act. These provisions do not apply to transfer of immovable property, held by the transferor as stock-in-trade.

A new section 43CA is inserted to provide that where the consideration for the transfer of an asset (other than capital asset), being land or building or both, is less than the stamp duty value, the value so adopted or assessed or assessable shall be deemed to be the full value of the consideration for the purposes of computing income under the head "Profits and gains of business or profession".

It is also provided that where the date of an agreement fixing the value of consideration for the transfer of the asset and the date of registration of the transfer of the asset are not same, the stamp duty value may be taken as on the date of the agreement for transfer and not as on the date of registration for such transfer. However, this exception shall apply only in those cases where amount of consideration or a part thereof for the transfer has been received by any mode other than cash on or before the date of the agreement.

27. COMPULSORY MAINTENANCE OF ACCOUNTS [SECTION 44AA]

Following assessee are required to maintain their accounts:

(a) In case of a specified profession:

- Every person carrying on specified profession shall keep and maintain such books of accounts and other documents as may enable the Assessing Officer to compute his total income in accordance with the provisions of this Act.

(b) In case of a business:

- If profits exceeds ₹ 1,20,000 or total sales or gross receipts exceed ₹ 10,00,000 in any of the 3 years immediately preceding the previous year or in case of new business, profits or total sales are likely to exceed the above said limit, then assessee need to maintain such books of accounts and other documents as may enable the AO to compute his taxable income in accordance with the Act.
- If profits or sales do not exceed above-mentioned limit in all of 3 previous years immediately preceding the previous year, then no books of accounts are required to be maintained.

Note:

- Person falling under section 44AD, 44AE, 44BB or 44BBB and claiming a lower income than specified in these sections also need to maintain such books of account and other documents as may enable the AO to compute their taxable income.
- Specified profession:** Every person carrying on legal, medical, engineering or architectural profession or the profession of accountancy or technical consultancy or interior decoration or authorised representative or film artist or any other profession as notified by the CBDT in the Official gazette.
- Books and documents required to be maintained under Rule 6F:** These are
 - Cash book;
 - Journal;
 - Ledger;
 - Copies of bills if amount is greater than ₹ 25;
 - A daily case register in Form No. 3C in case of person carrying on medical profession;
 - An inventory of drugs, medicines and other consumable accessories in case of person carrying on medical profession.

28. TAX AUDIT [SECTION 44AB]

Following assessees are required to get their accounts of previous year audited by a Chartered Accountant:

- (a) **In case of a business:** If total sales, turnover or gross receipts exceed ₹ 1 crore in any previous year; or
- (b) **In case of a profession:** if gross receipts exceed ₹ 25 lakhs in any previous year.

Note: Person falling under section 44AD, 44AE, 44BB or 44BBB and claiming a lower income than specified in these sections also need to get their accounts audited.

29. PRESUMPTIVE BASIS OF TAXATION FOR SMALL BUSINESS [SECTION 44AD]

This scheme is applicable to eligible assessees engaged in an eligible business.

Income from such business is estimated at 8% of total turnover or gross receipts in the previous year on account of such business or a sum higher than the above sum claimed to have been earned by the eligible assessee.

Eligible assessee means a resident individual, HUF or a partnership firm (other than LLP) and who has not claimed deduction u/s 10A, 10AA, 10B or deduction u/s 80IA, 80IAB, 80IB, 80IC, 80ID and 80IE, 80QQB, 80RRB, 80JJA, 80JJAA and 80LA.

Eligible business means any business except the business of plying, hiring or leasing goods carriages and whose total turnover or gross receipts in the previous year does not exceed an amount of ₹ 1 crore.

Notes:

- (a) The profits from business is computed on estimated basis assuming all the deductions under section 28 to 44D has been allowed to the assessee. Also, all disallowances from business income such as under Section 40, 40A or 43B, shall be deemed to have been adjusted from such business income.
- (b) Set off and carry forward provisions will apply against such profits as these are covered under section 70 to 80. However, unabsorbed depreciation shall not be adjusted against the above-mentioned profits as it is covered under section 32(2).
- (c) Deduction under section 80C to 80U can be claimed from such profits.
- (d) Assessee opting for the presumptive taxation need not comply with section 44AA or Section 44AB. If however, an assessee claims lower income than that specified above, then he must maintain books of accounts u/s 44AA and get its accounts audited u/s 44AB also.
- (e) In case of partnership firm, remuneration to partner and interest to partner will be allowed even if case falls under the above provision, under section 37 but subject to section 40b.
- (f) Eligible assessee of small business is not required to pay advance tax.
- (g) The provisions of Section 44AD shall not apply to:
 - (i) a person carrying on specified profession [sub-section 1 of Section 44AA];
 - (ii) a person carrying income in the nature of commission or brokerage;
 - (iii) a person carrying on any agency business.

30. PLYING, LEASING OR HIRING GOODS CARRIAGE [SECTION 44AE]

The scheme is applicable to all assessee whether resident or non-resident owning not more than 10 goods carriages at any time during the previous year.

Goods carriages may be taken on hire purchase/instalment also and the hirer in this case will be deemed owner of such goods carriage.

Deemed Business income in case of the business:

- (a) **In case of heavy vehicle:** Deemed profit is ₹ 5,000 per month (or part of the month) per heavy vehicle during which goods carriage is owned by the assessee or an amount claimed to have been actually earned from such vehicle, whichever is higher.
- (b) **In case of medium or light goods vehicle:** Deemed profit is ₹ 4,500 per month (or part of the month) per heavy vehicle during which goods carriage is owned by the assessee or an amount claimed to have been actually earned from such vehicle, whichever is higher.

Notes:

- (a) The profits from business is computed on estimated basis assuming all the deductions under section 28 to 44D has been allowed to the assessee. Also, all disallowances from business income such as under Section 40, 40A or 43B, shall be deemed to have been adjusted from such business income.
- (b) Set off and carry forward provisions will apply against such profits as these are covered under section 70 to 80. However, unabsorbed depreciation shall not be adjusted against the above-mentioned profits as it is covered under section 32(2).
- (c) Deduction under section 80C to 80U can be claimed from such profits.
- (d) Assessee opting for the presumptive taxation need not comply with section 44AA or Section 44AB. If however, an assessee claims lower income than that specified above, then he must maintain books of accounts u/s 44AA and get its accounts audited u/s 44AB also.
- (e) In case of partnership firm, remuneration to partner and interest to partner will be allowed even if case falls under the above provision, under section 37 but subject to section 40b.

Illustration

From the following profit and loss account of A for the year ended 31.3.2014, compute his gross total income for AY 2014-15:

Particulars	₹	Particulars	₹
Opening stock	8,00,000	Sales	140,00,000
Purchases	120,00,000	Closing stock	9,60,000
Salaries	16,00,000	Income from house property	160,000
Rent, rates and taxes	2,40,000	Dividends from an Indian company	18,000
Legal charges	80,000		
Miscellaneous expenses	40,000		
Provision for gratuity	40,000		
Provision for income tax	80,000		
Salary to Mrs. A	72,000		
Depreciation	80,000		
Reserve for bad debts	60,000		
Net Profits	46,000		
	<u>1,51,38,000</u>		<u>1,51,38,000</u>

Additional information:

- (i) Purchases include ₹2,00,000 paid in cash to a cultivator for purchase of an agricultural produce.
- (ii) Purchases also include ₹20,000 paid by way of compensation to a supplier as the assessee was unable to take the delivery of goods due to lack of storage space and finances.
- (iii) Opening stock was overvalued by 25% and closing stock was undervalued by 25%.
- (iv) Salary includes ₹30,000 paid as customary bonus on the occasion of Diwali over and above the bonus payable under the Payment of Bonus Act.
- (v) Rent, rates and taxes include ₹20,000 on account of disputed sales tax demand, ₹6,000 on account of municipal taxes for property let out. It also includes ₹10,000 as customs penalty paid during the year.
- (vi) An amount of ₹40,000 from a customer was written off from the provision for bad debts.
- (vii) An employee retired on 28.3.2014. Gratuity payable to him was ₹40,000. A provision was created for the same this year and it was paid on 2.4.2014.
- (viii) Mrs. A is a Commerce graduate and actively working in the assessee's firm.

Solution
**COMPUTATION OF GROSS TOTAL INCOME OF MR. A
FOR THE ASSESSMENT YEAR 2014-15 (PREVIOUS YEAR 2013-14)**

Particulars	₹
Net Profit as per Profit and Loss Account	46,000
Add: Inadmissible expenses if debited to Profit and loss account:	
– Disputed sales tax demand	20,000
– Municipal tax for property let out	6,000
– Customs penalty	10,000
– Reserve for bad debts	60,000
– Provision for income tax	80,000
– Overvaluation of opening stock	1,60,000
– Undervaluation of closing stock	<u>3,20,000</u>
	6,56,000
Less: Income taxable under any other head/exempt incomes, if credited to Profit and loss account	
– Income from house property	(1,60,000)
– Dividends from an Indian company	<u>(18,000)</u>
	(1,78,000)
Less: Admissible expenses if not debited to Profit & Loss Account	
– Bad debts	<u>(40,000)</u>
	(40,000)
Add: Taxable income if not credited to Profit and loss account	
	<u>Nil</u>
Total	4,84,000
<i>Add: Depreciation as per Profit and Loss Account</i>	
	80,000
<i>Less: Depreciation as per Income tax rules</i>	
	<u>80,000</u>
Business Income	4,84,000
Income from house Property:	
GAV (Actual rent)	1,60,000
<i>Less: Municipal taxes paid</i>	<u>(6,000)</u>
Net annual value (NAV)	1,54,000

Less: Deductions under section 24	
– Standard deduction @ 30% of NAV	<u>(46,200)</u>
Income from house property	<u>1,07,800</u>
Gross Total Income (Gross Total Income) (4,84,000 + 1,07,800)	<u>5,91,800</u>

Illustration

A, who is 28 years of age, is engaged in a business in Delhi. On the basis of the following profit and loss account for the financial year 2013-14, compute his taxable income:

Particulars	₹	Particulars	₹
Opening stock	20,700	Sales	15,00,000
Purchases	10,00,000	Closing stock	25,200
Household expenses	10,000		
Income tax for the FY 2013-14	30,000		
Interest on capital	8,400		
Depreciation on furniture	12,000		
Reserve for bad debts	1,200		
Salaries and wages	60,000		
Rent and rates	25,000		
Net Profits	<u>3,57,900</u>		
	<u>15,25,200</u>		<u>15,25,200</u>

Other relevant particulars are as follows:

- (i) Opening stock and closing stock have been consistently valued at 10% below cost price.
- (ii) Household expenses include a contribution of ₹1,500 towards Public Provident Fund.
- (iii) Amount of depreciation on furniture as per income-tax provisions is ₹10,000.

Assume that A has not opted for Section 44AD of the Act.

Solution

Computation of Gross Total Income of Mr. A for the Assessment year 2014-15 (Previous Year 2013-14)

Particulars	₹
Income under the head PGBP:	
Net Profit as per Profit and Loss Account	3,57,900
Add: Inadmissible expenses if debited to Profit and loss account:	
– Reserve for bad debts	1,200
– Interest on capital	8,400
– Income tax for the financial year 2013-14	30,000
– Household expenses	10,000
– Undervaluation of closing stock	<u>2,800</u>
	52,400

Less: Income taxable under any other head/exempt incomes, if

credited to Profit and loss account

Less: Admissible expenses if not debited to Profit & Loss Account

– Undervaluation of opening stock	<u>(2,300)</u>	(2,300)
<i>Add: Taxable income if not credited to Profit and loss account</i>	Nil	<u>Nil</u>
Total		4,08,000
<i>Add: Depreciation as per Profit and Loss Account</i>	12,000	
<i>Less: Depreciation as per Income tax rules</i>	<u>(10,000)</u>	
Business Income		4,10,000
Gross Total Income (Gross Total Income)		4,10,000
<i>Less: Deduction under section 80C (PPF)</i>	(1,500)	
Total Income		4,08,500

Note: For details, please refer the Tax Laws and Practice Executive Programme study material.

CAPITAL GAINS

CHARGEABILITY [SECTION 45]

Income will be chargeable as Capital gains if there is a capital asset and there is transfer of the capital asset during relevant previous year. (Section 45)

Capital Asset [Section 2(14)]: It means all assets except the following assets

- *Stock in Trade*
- *Personal movable assets (excluding jewellery, archaeological collections, antiques paintings, work of art)*
- *Rural agricultural land in India*
- *Gold deposit bonds*
- *Special bearer bonds*

Amendment in the definition of Capital Asset [by Finance Act, 2013]

The existing provisions contained in clause (14) of section 2 of the Income-tax Act define the term "capital asset" as property of any kind held by an assessee, whether or not connected with his business or profession. Certain categories of properties including agricultural land have been excluded from this definition. Sub-clause (iii) of clause (14) of section 2 provides that (a) agricultural land situated in any area within the jurisdiction of a municipality or cantonment board having population of not less than ten thousand according to last preceding census, or (b) agricultural land situated in any area within such distance not exceeding eight kilometers from the local limits of any municipality or cantonment board, as notified by the Central Government having regard to the extent and scope of urbanization and other relevant factors, forms part of capital asset.

Item (b) of sub-clause (iii) of clause (14) of section 2 is amended so as to provide that the land situated in any area within the distance, measured aerially (shortest aerial distance)

- (I) not being more than two kilometers, from the local limits of any municipality or cantonment board

- referred to in item (a) and which has a population of more than ten thousand but not exceeding one lakh; or
- (II) not being more than six kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than one lakh but not exceeding ten lakh; or
- (III) not being more than eight kilometers, from the local limits of any municipality or cantonment board referred to in item (a) and which has a population of more than ten lakh, shall form part of capital asset.

The expression "population" is also defined to mean population according to the last preceding census of which the relevant figures have been published before the first day of the previous year.

Similar amendments are also made in clause (1A) of section 2 of the Income-tax Act, 1961 relating to the definition of "agricultural income" and in respect of the definition of "urban land" in the Wealth-tax Act, 1957.

Transfer

Section 2(47) defined the word Transfer. Transfer includes:

- Sale, Exchange or Relinquishment of the asset or
- Extinguishment of any right therein or
- Compulsory Acquisition thereof under any law or
- Conversion of Capital asset into Stock in Trade or
- The maturity or redemption of Zero Coupon bonds

Section 47 of the income tax Act provide exceptions for the transactions which are not treated as transfer.

Year of Chargeability

Capital gain arising on transfer of a capital asset is chargeable to tax in the year of transfer. However, in following cases, capital gain will be charged to tax in the year of receipt:

- Insurance compensation
- Conversion of Capital Asset into Stock in Trade
- Compulsory acquisition of the property

Type of Capital Asset and Capital Gain

Capital asset can be short term or long term depending upon the period of holding (i.e. date of acquisition to one day prior to date of transfer)

Short term Capital asset

A capital asset will be a short term capital asset if period of holding of such capital asset is 36 months or less. However, in case of financial assets, a capital asset is short term capital asset if its period of holding is 12 months or less.

Financial assets are Shares, Units of Mutual Funds, Listed securities, Govt securities and zero coupon bonds

Note: Depreciable assets will always be Short term capital assets.

Gain arising on transfer of Short term capital assets is known as short term capital gain.

Long term Capital asset

A capital asset is a long term capital asset if Period of holding is more than 36 months.

However, in case of financial assets, an asset will be long term capital asset if its period of holding is more than 12 months.

Note: Gain arising on transfer of Long term capital asset is Long term capital gains.

Computation of STCG

Particulars	Amount (in ₹)
Sale consideration	XXX
<i>Less: Cost of Acquisition (COA)</i>	(XXX)
<i>Less: Cost of Improvement (COI)</i>	(XXX)
<i>Less: Expenses on Transfer</i>	<u>(XXX)</u>
STCG	XXX
<i>Less: Exemptions</i>	<u>(XXX)</u>
Taxable STCG	<u>XXX</u>

Computation of LTCG

Particulars	Amount (in ₹)
Sale consideration	XXX
<i>Less: Indexed Cost of Acquisition (COA)</i>	(XXX)
<i>Less: Indexed Cost of Improvement (COI)</i>	(XXX)
<i>Less: Expenses on Transfer</i>	<u>(XXX)</u>
LTCG	XXX
<i>Less: Exemptions</i>	<u>(XXX)</u>
Taxable LTCG	<u>XXX</u>

Notes: COA = Purchase price + brokerage on acquisition

EXEMPTIONS

Particulars	Sec 54	Sec 54B	Sec 54F	Sec 54EC	Sec 54GA
Allowed to	Individual HUF	Individual	Individual HUF	Any Assessee	Any Assessee
Asset transferred	Long Term Residential House Property	Long term/Short term Urban Agricultural Land Atleast 2 year old and used by assessee/parents	Any Long Term Capital Assets other than Residential House Property	Any Long Term Capital Assets	Short Term/Long Term Land, Building, Plant in Urban Area

New Asset to be acquired	Residential House Property	Agricultural Land Urban/Rural	Residential House Property	Bonds of National Highway Authority of India or Residential Electrification Corporation Ltd. (Lock in period: 3 years)	Land, Building, Plant in SEZ
Time limit for Acquisition of new asset	Purchase within 1 year before or 2 years after the date of transfer Construction: within 3 years after the date of transfer	Purchase within 2 years after the date of transfer	Purchase within 1 year before or 2 years after the date of transfer Construction: within 3 years after the date of transfer	Within 6 months from date of transfer	Purchase/ Construction: within 1 year before or 2 years after the date of transfer
Deposit scheme	Applicable	Applicable	Applicable	NA	Applicable
Eligible Amount	(Purchased/Construction + Amount Deposited) Upto due date of Return of Income	(Purchased + Amount deposited) upto due date of Return of Income	(Purchased/Construction + Amount Deposited) upto due date of Return of Income	Purchase upto specified date (Maximum investment: ₹ 50 lakhs)	(Purchased/Construction + Amount Deposited) upto due date of Return of Income
Exemption	Lower of: Long term Capital Gain or Eligible Amount	Lower of: LTCG/STCG or Eligible Amount	LTCG/NSC Eligible Amount	Lower of LTCG or Eligible amount	Lower of: LTCG/STCG or Eligible Amount
Consequences of unutilization of Deposit	LTCG exempted earlier taxable. YOC = transfer date + 3 year	LTCG/STCG exempted earlier taxable. YOC = transfer date + 2 year	Proportionate LTCG exempted earlier taxable. YOC = transfer date + 3 year	NA	LTCG exempted earlier taxable. YOC = transfer date + 3 year
Consequences of new asset transfer within 3 years	STCG will arise; Cost of Acquisition will be reduced by LTCG exempted earlier.	STCG will arise; COA will be reduced by LTCG/STCG exempted earlier.	STCG will be calculated. LTCG exempted earlier taxable as LTCG in the year of transfer.	STCG will be calculated. LTCG exempted earlier taxable as LTCG in the year of transfer.	STCG will arise; COA will be reduced by LTCG exempted earlier.

Note: For details please refer the Tax Laws and Practice Executive Programme Study Material.

INCOME FROM OTHER SOURCES

CHARGING SECTION (SECTION 56)

Income not chargeable to tax under any of the first four heads is chargeable under the head "Income from other sources". (Section 56)

Method of Accounting: Under this head, the assessee has the option of computing its income either by following mercantile or cash basis of accounting.

LIST OF INCOMES TAXABLE UNDER INCOME FROM OTHER SOURCES

Section 56(2) provides list of certain incomes which are charged to tax as income from other sources.

(i) Taxability of Dividends [Section 56(2)(i)]

Dividend income is always taxable as Income from other sources whether shares are held as stock in trade or as an investment. For the purpose of set off of losses, dividend income shall be treated as business income. Deduction in connection with earning such income like interest and collection charges are allowed as deduction.

(ii) Taxability of Interest on securities [Section 56(2)(id)]

Where securities are held as investment, then interest is chargeable under the head Income from other sources. Deduction shall be allowed under section 56 to 59 of the Act in respect of such income.

Deduction in the nature of expenditure incurred for earning interest and collection charges are allowed as deduction for computing such income.

Interest is chargeable to tax as per the method of accounting (i.e. mercantile or cash) followed by the assessee.

Interest on securities falls due on the date specified by the issuing authority. Whole of interest which falls due on the due date is chargeable to tax for that person even if securities are held by him for a day.

(iii) Taxability of Family Pension

Family pension received by the legal heirs of the deceased employee is taxable in the hands of the recipient. A deduction of lower of 1/3rd of the pension or ₹ 15,000 is allowed as deduction for the recipient.

(iv) Taxability of money received on Keyman Insurance Policy

Where maturity amount is received by the legal heir on the death of employee under keyman insurance policy, then such amount is taxable as Income from other sources in the hands of recipient.

(v) Taxability of Income from letting out of plant and machinery, furniture [Section 562(ii)]

These profits/incomes would be taxable as income from other sources if not charged to tax as business or profession income. Depreciation is allowed as deduction.

(vi) Taxability of Income from composite letting of plant and machinery, furniture with building [Section 56(2)(ii)]

If letting of building is inseparable from the letting of the said machinery, plant or furniture, then income from such letting is charged to income-tax as income from other sources. Depreciation is allowed as deduction.

(vii) Taxability of Casual Income [Section 56(2)(ib)]

Casual income (like lottery or winning from card games or other games of any sort) is chargeable to tax as income from other sources. No deduction is allowed in respect of such income. Further, deduction under section 80C to 80U is also not allowed as deduction. Casual income is taxable @ 30% flat rate (and surcharge and cess, as applicable).

(viii) Taxability of profit from activity of owning and maintaining race horses [Section 56(2)]

Such profits are chargeable as income from other sources. Any allowances or expenses incurred in connection with the activity of owning and maintaining race horses is allowed as deduction.

(ix) Taxability of Gifts [Section 56(2)(vii)]**(a) Gift of Money**

Where an Individual or a HUF receives in any previous year from any person or persons on or after 1/10/2009 any sum of money, without consideration, the aggregate value of which exceeds ₹ 50,000 then the whole of the aggregate value of such sum is chargeable under the head "Income from other sources".

Exceptions

However, this clause shall not apply in following cases:

(a) Gifts received from any relative on any occasion is not taxable.

Relative for above purposes include following:

In case of Individual:

- (i) Spouse of the individual;
- (ii) Brother or sister of the individual;
- (iii) Brother or sister of the spouse of the individual;
- (iv) Brother or sister of either of the parents of the individual;
- (v) Any Lineal ascendant or descendant of the individual;
- (vi) Any lineal ascendant or descendant of the spouse of the individual, and
- (vii) Spouse of a person referred to in items (ii) to (vi) above.

In case of a Hindu Undivided Family, any member thereof.

- (b) Gifts received from any person on the occasion of the marriage of the individual is not taxable;
- (c) Gifts received under a will or by way of inheritance is not taxable;
- (d) Gifts received in contemplation of death of the payer is not taxable;
- (e) Money received from local authority, any fund, foundation, university, other educational institution, hospital, medical institution, any trust or any institution referred to in section 10(23C) and money received from a charitable trust registered under section 12AA is not taxable.

(b) Gift of Immovable Property

Where an individual or a HUF receives in any previous year, from any person or persons on or after 1/10/2009, any immovable property (being a capital asset) without consideration, the stamp duty value of which exceeds ₹ 50,000, then the stamp duty value of such property is taxable as Income from other sources.

Exceptions: Further, the exceptions as applicable for gift of money, will also apply in case of gift of immovable property.

(c) Taxability of Immovable Property Received for Inadequate Consideration [Finance Act, 2013]

The existing provisions of sub-clause (b) of clause (vi) of sub-section (2) of section 56 of the Income-tax Act, *inter alia*, provide that where any immovable property is received by an individual or HUF without consideration, the stamp duty value of which exceeds fifty thousand rupees, the stamp duty value of such property would be charged to tax in the hands of the individual or HUF as income from other sources.

The existing provision does not cover a situation where the immovable property has been received by an individual or HUF for inadequate consideration. The provisions of clause (vi) of sub-section (2) of section 56 are amended so as to provide that where any immovable property is received for a consideration which is less than the stamp duty value of the property by an amount exceeding fifty thousand rupees, the stamp duty value of such property as exceeds such consideration, shall be chargeable to tax in the hands of the individual or HUF as income from other sources.

Considering the fact that there may be a time gap between the date of agreement and the date of registration, it is provided that where the date of the agreement fixing the amount of consideration for the transfer of the immovable property and the date of registration are not the same, the stamp duty value may be taken as on the date of the agreement, instead of that on the date of registration. This exception shall, however, apply only in a case where the amount of consideration, or a part thereof, has been paid by any mode other than cash on or before the date of the agreement fixing the amount of consideration for the transfer of such immovable property.

(d) Gift of Movable Property

Where an individual or a HUF receives, in any previous year, from any person or persons on or after 1.10.2009 any specified movable property being capital asset without consideration, the aggregate fair market value of which exceeds ₹ 50,000, then the whole of the aggregate fair market value of such property is taxable as income from other sources.

However, if such asset is received for a consideration which is less than the aggregate fair market value of the property by an amount exceeding ₹ 50,000, the aggregate fair market value of such property as exceeds such consideration is taxable as income from other sources.

Specified Movable property: Jewellery; Archaeological collections; Drawings; Paintings; Bullion; Sculptures; Any work of art; Shares and Securities.

Fair market value means the value determined in accordance with the prescribed method.

Exceptions: The exceptions as applicable for gift of money, will also apply in case of gift of immovable property.

(e) Gifts of shares of closely held company to firm or to closely held company [Section 56(2)(viiia)]

Where a firm or a company not being a company in which the public is substantially interested, receives, in any previous year, from any person or persons, on or after 1.6.2010, any property being shares of a company not being a company in which the public is substantially interested, without consideration, the aggregate FMV of which exceeds ₹ 50,000 then the entire FMV is taxable as income from other sources.

If such shares are received for a consideration which is less than the aggregate of FMV of the property by an amount exceeding ₹ 50,000, then the aggregate FMV of such property as exceeds such consideration will be

taxable as income from other sources.

(f) Share premium in excess of the fair market value to be treated as income [Section 56(2)(viib)]

Where a company, not being a company in which the public are substantially interested, receives, in any previous year, from any person being a resident, any consideration for issue of shares that exceeds the face value of such shares, the aggregate consideration received for such shares as exceeds the fair market value of the shares shall be taxable under Income from other sources.

However, that this clause shall not apply where the consideration for issue of shares is received:

- (i) by a venture capital undertaking from a venture capital company or a venture capital fund; or
- (ii) by a company from a class or classes of persons as may be notified by the Central Government in this behalf.

Accordingly, it is provided that the fair market value of the shares shall be the higher of the value—

- as may be determined in accordance with the method as may be prescribed; or
- as may be substantiated by the company to the satisfaction of the Assessing Officer, based on the value of its assets, including intangible assets, being goodwill, know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of similar nature.

DEDUCTIONS [SECTION 57]

Any expenditure (other than capital expenditure) laid out or expended wholly and exclusively for the purpose of making or earning incomes taxable under this head, is allowed as deduction.

INADMISSIBLE EXPENSES [SECTION 58]

Following expenses are not allowed:

- Personal expenses of the assessee;
- Interest and salary payable outside India, if tax is not deducted or after deduction, has not been paid;
- Wealth tax;
- Expenses of the nature specified under section 40A of the Act;
- Any expenditure or allowance in respect of winning from lotteries, crossword puzzles, races, card games, including horse race etc.

OTHER INCOMES CHARGEABLE AS INCOME FROM OTHER SOURCES

- (a) Fees for attending the Board meetings (other than that received by Whole time or Executive director);
- (b) Examinership remuneration received otherwise in capacity of an employee;
- (c) Remuneration received by MPs or MLAs;
- (d) Income from subletting of a house property;
- (e) Rent from a vacant piece of land;
- (f) Interest on bank deposits or on deposits with companies;
- (g) Insurance commission;

- (h) Agricultural income from outside India;
- (i) Royalty income, if not taxable as business income
- (j) Interest on delayed refund of income tax.

Note: For details please refer the Tax Laws and Practice Study Material of Executive Programme.

CLUBBING OF INCOME

The following are provisions for clubbing of income:

(i) Transfer of Income without transfer of assets (Section 60)

Income in this case is clubbed in the hands of transferor always.

(ii) Remuneration to spouse

Remuneration received by spouse from a concern in which individual has Substantial Interest (atleast 20% voting power or share in profits along with relatives) will be clubbed in the hands of that spouse who has Substantial interest.

If both the spouses have Substantial Interest then, remuneration would be clubbed in the hands of spouse whose total income excluding remuneration is greater

Income will not be clubbed where the remuneration is reasonable, as per the knowledge, experience etc.

(iii) Clubbing provisions relating to spouse or son's wife

Income from asset transferred for inadequate consideration to spouse/son's wife/third person (for the benefit of spouse or son's wife) to be clubbed in the hands of transferor

Relationship must exists both at the time of transfer of assets and at the time when income accrues.

Clubbing of income would not be done in case of transfer of an asset without adequate consideration to spouse if transfer is in an agreement to live apart.

(iv) Minor's child Income

If marriage of parent subsists then Minor's income is to be clubbed in the hands of that parent whose income excluding minor's income is greater.

If marriage of parent does not subsist: Minor's income to be clubbed in the hands of that parent who maintains the minor child during relevant previous year.

Clubbing provisions do not apply if minor is disabled or minor is earning income by way of skill, knowledge etc.

Exemption upto ₹1500 is allowed to parent in whose income minor's income is clubbed.

(v) Revocable transfer of asset

Income from revocable transfer of asset is to be clubbed in the hands of transferor.

(vi) Income from self acquired property converted to HUF property

Income from an asset transferred by member to HUF will be taxable in the hands of the Member only. On partition, member's share and spouse's share in property would be taxable.

SET OFF AND CARRY FORWARD OF LOSSES

SET OFF OF LOSSES

Losses under the following heads are allowed to be adjusted against same head of income or any other head of income in the previous year of loss (Set off of losses). If losses are not set off in the current previous year, then these will be carried forward and set off in subsequent previous year:

- Loss from house property;
- Loss from business or profession;
- Capital losses
- Loss from other sources.

There can be no loss from the Salary.

RULE OF SET OFF AND CARRY FORWARD

First of all, for the losses of previous year, set off provisions will apply (i.e Intra-head adjustment under section 70 or Inter-head adjustment under section 71). If losses cannot be set off in the current previous year, then these will be carried forward to subsequent previous year to be set off against income from same head of income.

Rules relating to set off and carry forward of losses for each source of income are as under:

Loss from house property

- **Intra-head adjustment (Section 70):** Loss of current previous year is allowed against income from house property.
- **Inter-head adjustment (Section 71):** Loss, if not set off, from income from house property will be set off against income under any other head of income.
- **Carry forward and set off (Section 71B):** Loss, if not set off in the relevant previous year, will be carried forward to be set off in 8 subsequent assessment years only against income from house property.
- Loss can be carried forward even if return is not filed upto due date of return of Income as section 80 is not applicable.

Business losses

- **Intra-head adjustment (Section 70):** Speculation loss can only be set off against speculative business income. Loss from non-speculative business can be set off against profits from speculative as well as non-speculative business.
- Speculative transaction is defined under section 43(5) as a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by the actual delivery or transfer of the commodity or scrips.
- **Inter-head adjustment (Section 71):** Speculative business loss cannot be set off against income from any other head of income. However, loss from non speculative business can be set off against income from any other head except "Salaries".
 - Non speculative business loss can be carried forward and set off in subsequent 8 Assessment years against speculative or non-speculative business income only [Section 72].

- Speculative business loss can be carried forward and set off in subsequent 4 Assessment Years against speculative business profits only [Section 73].

As per section 80, the return of loss should be filed upto due date of return of income in order to carry forward and set off the above-mentioned losses.

Notes:

- The business in respect of which a loss is incurred need not be continued (not applicable for speculative business loss).
- Loss can be set off only by that assessee who has incurred the loss (No exception for speculative business loss). However, there are following exceptions to this rule:
 - Accumulated business loss of amalgamating company can be carried forward and set off by amalgamated company [Section 72A];
 - Accumulated business loss of demerged company can be carried forward and set off by resulting company [Section 72A];
 - In case of conversion of proprietorship or partnership concern into a company, loss can be carried forward and set off by succeeding company [Section 72A];
 - Conversion of Private limited company or unlisted company to LLP [Section 72A];
 - Losses of business acquired on inheritance under section 78(2).

- Carry forward and set off of unabsorbed depreciation [Section 32(2)]:** The unabsorbed depreciation means depreciation which is not absorbed by the profits of the business. There cannot be any loss under the head PGBP because of depreciation.

The unabsorbed depreciation can be set off with any head of income except casual income and salary. However, it shall first be set off against business income. It shall be carried forward for indefinite period. It is allowed to be carried forward even if return of income is not filed upto due date of return of income. Also, the business in respect of which there is unabsorbed depreciation need not be continued.

- Priority of set off of losses:** Following order need to be followed while setting off of business losses and unabsorbed expenditures:
 - Current scientific expenditure [Section 35], Current capital expenditure on family planning [Section 36(1)(ix)] and current depreciation [Section 32];
 - Brought forward business loss under section 72;
 - Unabsorbed capital expenditure on family planning u/s 36(1)(ix), unabsorbed depreciation u/s 32(2) and unabsorbed scientific research expenditure u/s 35(4).

Capital Losses

Intra-head adjustment (Section 70): Short term capital losses can be set off against short term or long term capital gains. However, long term capital losses can be set off only against Long term capital gains.

Inter-head adjustment (Section 71): Capital losses cannot be set off against income from any other head of income.

Carry forward and set off (Section 74): Short term capital losses can be carried forward to next 8 assessment years to be set off against short term or long term capital gains. However, long term capital losses can be carried forward to next 8 assessment years to be set off against long term capital gains.

As per section 80, the return of loss should be filed upto due date of return of income in order to carry forward and set off the above-mentioned losses.

Other losses

Intra-head adjustment (Section 70): Loss from the activity of owning and maintaining race horses can be set off from the profit of same type of activity only. Casual losses (i.e. losses from races, lotteries, crossword puzzles etc.) are neither allowed to be set off nor to be carried forward and also, income from these cannot be used to set off any type of losses. Other losses can be set off from any income from other sources.

Intra-head adjustment (Section 71): Loss from the activity of owning and maintaining race horses can be set off from the profit of same type of activity only. Casual losses (i.e. losses from races, lotteries, crossword puzzles etc.) are neither allowed to be set off nor to be carried forward and also, income from these cannot be used to set off any type of losses. Other losses can be set off from any income from other sources.

Loss from activity of owning and maintaining horses (Section 74A): Loss from the activity of owning and maintaining race horses can be carried forward to subsequent 8 assessment years to be set off from the profit of same type of activity only. As per section 80, the return of loss should be filed upto due date of return of income in order to carry forward and set off the above-mentioned losses.

Other losses cannot be carried forward.

Set off of Losses in case of Amalgamation [Section 72A(1)]

In case of an amalgamation, losses of amalgamating company will be treated as losses of amalgamated company of the previous year in which amalgamation has taken place and will be set off and carried forward by the amalgamated company provided the following conditions are satisfied.

Conditions to be satisfied by Amalgamating company

There has been an amalgamation of a company owning an industrial undertaking and the amalgamating company is engaged in the business for 3 years or more and it has held continuously as on the date of amalgamation at least 75% of the book value of fixed assets held by it 2 years prior to the date of amalgamation.

Conditions to be satisfied by Amalgamated company

1. It continues to hold at least 75% of the book value of fixed assets of the amalgamating company for a minimum period of 5 years from the date of acquisition; and
2. It continues the business of the amalgamating company for a minimum period of 5 years from the date of amalgamation; and
3. A report of CA is furnished.

Losses of Closely Held Companies [Section 79]

A closely held company (a company in which the public is not substantially interested) incurs a loss in any year and such company can carry forward and set off such loss only if on the last day of the previous year in which loss is incurred and last day of the previous year in which loss is set off, at least 51% of the voting power were beneficially held by same persons.

However, losses are allowed to be carried forward and set off even if conditions of 51% is not satisfied and there is a change in the voting power consequent to the following situations:

- (a) On the death of a shareholder; or

(b) On account of transfer of shares by way of gifts to any relative of the shareholder making such gift.

These provisions do not apply to unabsorbed depreciation.

DEDUCTIONS FROM GROSS TOTAL INCOME U/S 80C TO 80U

As per **Section 80A**, deductions under section 80C to 80U cannot exceed Gross Total Income (GTI).

DEDUCTION UNDER SECTION 80C

It is available only to Individual or HUF. As per Section 80C, deduction is allowed in that year in which specified investment or expenditure is made. Amount can be deposited or paid out of any income, i.e. exempted as well as borrowed funds also.

Specified investments/deposits: Contribution to

(a) **Life Insurance premium:** Paid by Individual or HUF towards life insurance premium on the life of spouse and any child or any member of HUF. However, maximum deduction will be allowed upto 10% of the actual capital sum assured.

As per section 10(10D), any sum received under a life insurance policy including the sum allocated by way of bonus on such policy is exempt if premium payable for all the years during the term of the policy do not exceed 10% of the actual capital sum assured. However, any sum received on death of a person from LIC is fully exempt from tax.

- (b) Unit Linked Insurance Plan of UTI or Mutual Fund registered in India;
- (c) Fixed Deposit of at least 5 years with a scheduled bank;
- (d) Fixed Deposit for 5 years by an individual in an account under Post Office Time Deposit Rules 1981.
- (e) Equity Linked saving scheme of UTI or Mutual Fund.
- (f) Contribution made by an Individual to SPF or RPF;
- (g) Public Provident Fund;
- (h) Approved superannuation fund;
- (i) NSC VIII issue (including interest accrued thereon);
- (j) Subscription to shares or debentures or bonds of an issue by Indian public company or a public financial institution etc. the entire proceeds of which is utilised wholly and exclusively for the purposes of developing, maintaining and operating an infrastructure facility or for generating or/and distributing, power or for providing telecommunication services.
- (k) Any payment made towards the cost of purchase or construction of residential house property (repayment of housing loan);
- (l) Tuition fees of maximum 2 children;
- (m) Deposits in an account under the Senior citizens Savings Schemes;
- (n) Any contribution made by Individual or HUF as subscription to Home Loan Account Scheme of National Housing Bank (NHB);
- (o) Contribution to any notified pension fund set up by the NHB or Mutual fund or UTI;
- (p) Subscription made by Individual or HUF to any such deposit scheme of a public sector company or an approved authority engaged in providing long term finance for construction or purchase of houses in India for residential purposes.

As per Section 80CCE, maximum deduction allowed under section 80C, 80CCC and 80CCD can be ₹ 1 lakh only.

AMENDMENT IN SECTION 80C [FINANCE ACT, 2013]

Sub-section (3A) of section 80C is amended so as to provide that the deduction under the said section on account of premium paid in respect of a policy issued on or after 01.04.2013 for insurance on the life of a person referred to above shall be allowed to the extent the premium paid does not exceed 15% of the actual capital sum assured. (Amendment by Finance Act, 2013)

Further, it is provided that any sum including the sum allocated by way of bonus received under an insurance policy issued on or after 01.04.2013 for the insurance on the life of any person who is:

- (i) a person with disability or a person with severe disability as referred to in section 80U, or
- (ii) suffering from disease or ailment as specified in the rules made under section 80DDB,

shall be exempt under clause (10D) of section 10 if the premium payable for any of the years during the term of the policy does not exceed 15% of the actual capital sum assured. [Amendment by Finance Act, 2013]

"actual capital sum assured" in relation to a life insurance policy shall mean the minimum amount assured under the policy on happening of the insured event at any time during the term of the policy, not taking into account--

- (I) the value of any premium agreed to be returned; or
- (ii) any benefit by way of bonus or otherwise over and above the sum actually assured, which is to be or may be received under the policy by any person.

CONTRIBUTION TO PENSION FUND OF LIC OR PRIVATE INSURER [SECTION 80CCC]

Deduction is allowed to an Individual only where the deposit is made in any pension plan of LIC or any other private insurer for receiving pension from the fund set up by the said corporation.

Deduction is lower of contribution or ₹ 1,00,000.

Contribution has to be made from income chargeable to tax. Surrender value received is taxable in the year of receipt in the hands of the assessee or nominee.

CONTRIBUTION TO PENSION FUND [SECTION 80CCD]

Deduction is allowed to an Individual (salaried class or self employed person) under the New Pension scheme set up under NPS trusts.

Deduction in case of salaried employees is aggregate of the amount contributed by such individual (upto 10% of superannuation salary) and the amount contributed by the employer (upto 10% of superannuation salary) in the previous year.

Superannuation salary includes dearness allowance, if the terms of employment so provide, but excludes all other allowances and perquisites.

Deduction in case of self employed is lower of the contribution and 10% of Gross total income (GTI).

DEDUCTION IN RESPECT OF INVESTMENT MADE UNDER AN EQUITY SAVINGS SCHEME [SECTION 80CCG] [FINANCE ACT, 2013]

- (1) Where an assessee, being a resident individual, has, in a previous year, acquired listed equity shares [or

listed units of an equity oriented fund] in accordance with a scheme, as may be notified by the Central Government in this behalf, he shall, subject to the provisions of sub-section (3), be allowed a deduction, in the computation of his total income of the assessment year relevant to such previous year, of fifty per cent of the amount invested in such equity shares [or units] to the extent such deduction does not exceed twenty-five thousand rupees.

(2) The deduction under sub-section (1) shall be allowed in accordance with, and subject to, the provisions of this section for three consecutive assessment years, beginning with the assessment year relevant to the previous year in which the listed equity shares or listed units of equity oriented fund were first acquired.

(3) The deduction under sub-section (1) shall be subject to the following conditions, namely:—

- (i) the gross total income of the assessee for the relevant assessment year shall not exceed [ten] lakh rupees;
- (ii) the assessee is a new retail investor as may be specified under the scheme referred to in sub-section (1);
- (iii) the investment is made in such listed equity shares [or listed units of equity oriented fund] as may be specified under the scheme referred to in sub-section (1);
- (iv) the investment is locked-in for a period of three years from the date of acquisition in accordance with the scheme referred to in sub-section (1); and
- (v) such other condition as may be prescribed.

(4) If the assessee, in any previous year, fails to comply with any condition specified in sub-section (3), the deduction originally allowed shall be deemed to be the income of the assessee of such previous year and shall be liable to tax for the assessment year relevant to such previous year.]

Explanation.—For the purposes of this section, "equity oriented fund" shall have the meaning assigned to it in the Explanation to clause (38) of section 10.

CONTRIBUTION TOWARDS HEALTH INSURANCE PREMIUM [SECTION 80D]

- (1) In computing the total income of an assessee, being an individual or a Hindu undivided family, there shall be deducted such sum, as specified in sub-section (2) or sub section (3), payment of which is made by any mode as specified in the previous year out of his income chargeable to tax.
- (2) Where the assessee is an **individual**, the sum referred in sub section(1) shall be the aggregate of the following:
 - (a) The whole of the amount paid to effect or to keep in force an insurance on the health of the assessee or his family or "any contribution made to the Central Government Health Scheme" or such other scheme as may be notified by the Central Government in this behalf or any payment made on account of preventive health check-up of the assessee or his family and the sum does not exceed in the aggregate ₹15,000; and
 - (b) The whole of the amount paid to effect or to keep in force an insurance on the health of the parent or parents of the assessee or any payment made on account of preventive health check-up of the parent or parents of the assessee and the sum does not exceed in the aggregate ₹15,000.

The deduction in respect of payment made on account of **preventive health check-up** shall not exceed ₹ 5,000.

Explanation: Family means the spouse and the dependent children of the assessee.

Payment shall be made by any mode, including cash, in respect of any sum paid on account of preventive health check-up and by any mode other than cash in all cases other than preventive health check-up.

- (3) Where the assessee is a **Hindu undivided family**, the sum referred to in sub-section (1) shall be the whole of the amount paid to effect or to keep in force an insurance on the health of any member of that Hindu undivided family as does not exceed in the aggregate ₹15,000.
- (4) In case of a senior citizen the amount shall not exceed ₹20,000.

Explanation: For the purpose of this sub section, senior citizen means an individual resident in India who is of the age of sixty years or more at any time during the relevant previous year.

MAINTENANCE INCLUDING MEDICAL TREATMENT OF A DEPENDANT WHO IS A PERSON WITH DISABILITY [SECTION 80DD]

Deduction is available to a resident Individual/HUF who maintains disabled dependant person.

A disabled dependant means a person who in the case of an Individual may be Spouse, children, parents, brothers and sisters of the individual or any of them and in the case of a HUF, it may be a member of the HUF who is dependant wholly or mainly on such individual or HUF for his support and maintenance and is not dependant on any person other than such Individual or HUF for his support or maintenance and is suffering from permanent physical disability certified by a Medical Authority.

Amount of deduction: Deduction is allowed as follows:

- (a) ₹ 50,000 fixed deduction irrespective of expenditure incurred;
- (b) ₹ 1,00,000 fixed deduction in case of person with severe disability.

Meaning of disability: Blindness, Low vision, Leprosy cured, Hearing Impairment, Locomotor disability, Mental retardation and mental illness.

Person with disability: It means a person suffering from not less than 40% of any disability as certified by a medical authority.

Person with severe disability: it means a person with 80% or more of one or more disabilities.

Note:

If the disabled dependant predeceases the assessee, an amount withdrawn shall be deemed to be the income of the assessee of the previous year in which such amount is withdrawn.

Double benefit of section 80DD and 80U is not available.

DEDUCTION TO DISABLED INDIVIDUAL [SECTION 80U]

Deduction is available to a resident individual who is completely blind or suffers from permanent physical disability certified by a Medical Authority.

Amount of deduction:

- (a) ₹ 50,000 deduction is allowed irrespective of expenditure incurred;
- (b) ₹ 1,00,000 deduction is allowed in case of person with severe disability.

Double benefit of section 80DD and 80U is not available.

DONATIONS [SECTION 80G]

Deduction is available to all assessees who make donation in specified fund. Deduction under this section is allowed in some case @ 100% without qualifying limit or with qualifying limit and @ 50% with or without qualifying limit.

(I) Any amount donated irrespective of the gross total income is eligible for deduction. The deduction allowed is either 100% of donation made or 50% of donation made.

Fund	Deduction allowed
National Defence Fund	100%
The Army Central Welfare Fund or The Air Force Central Welfare Fund	100%
National Sports Fund set up by the Central Government	100%
National Cultural Fund set up by the Central Government	100%
National Foundation for Communal Harmony	100%
National State Blood Transfusion Council	100%
National Illness Assistance Fund	100%
Zila Saksharta Samiti	100%
Prime Minister's National Relief Fund	100%
National Eminent University/Educational Institution approved by the prescribed authority	100%
Fund of Technology Development and Application set up by the Central Government	100%
National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple Disabilities	100%
National Children Fund	100%
Prime Minister's Drought Relief Fund	50%
Jawaharlal Nehru Memorial Fund	50%
Indira Gandhi Memorial Trust	50%
Rajiv Gandhi Foundation	50%

(II) Where maximum permissible limit is specified to the fund. Maximum permissible limit is 10% of Adjusted Total Income.

Fund	Deduction allowed
Donation to Government/Approved Local Authority, Institution to be utilised for promoting family planning	100%
Donation to be utilised for charitable purpose	50%
Any notified temple, mosque, gurudwara, church or other place	50%
Donation made by a company to the Indian Olympic association or to an Institute notified u/s 10(23G) for the development of infrastructure for sports in India or for sponsorship of sports or games in India	100%

Adjusted Total Income: Gross Total Income – Special Incomes [Long term capital gains and Short term capital gains (on STT paid securities)] – Deductions under section 80C to 80U except under section 80G.

AMENDMENT IN SECTION 80G [FINANCE ACT, 2013]

With effect from assessment year 2013-14, Section 80G has been amended so as to specify therein that any payment exceeding a sum of ten thousand rupees shall only be allowed as a deduction if such sum is paid by any mode other than cash.

DEDUCTION IN RESPECT OF RENT PAID [SECTION 80GG]

Deduction is allowed to an Individual who lives in a rented accommodation provided by the employer or otherwise and who is not in receipt of HRA. Also, the individual, his spouse, minor child or the HUF of which he is a member must not own any residential house property at the place where he works or if he owns then he should not claim any concession in respect of self occupied house for residence under section 23(2).

Amount of deduction: The least of following shall be allowed as deduction:

- ₹2,000 per month;
- 25% of Adjusted Total Income;
- Rent paid – 10% of Adjusted Total Income.

Adjusted Total Income: Gross Total Income – Special Income – Deductions under section 80C to 80U except 80GG.

INTEREST ON LOAN TAKEN FOR HIGHER EDUCATION [SECTION 80E]

Deduction is available to an Individual who has taken a loan for his own higher education (higher education means any course of study pursued after pursuing XIIth including vocational studies) or higher education of his relative (spouse and children) from any Financial Institution or Banking company or any approved charitable institution.

Deduction: Any amount paid by the assessee in the PY by way of payment of interest. This deduction is allowed from the year the assessee starts payment of interest and subsequent 7 assessment year.

DEDUCTION IN RESPECT OF INTEREST ON LOAN TAKEN FOR RESIDENTIAL HOUSE PROPERTY [SECTION 80EE INTRODUCED BY FINANCE ACT, 2013]

(1) In computing the total income of an assessee, being an individual, there shall be deducted interest payable on loan taken by him from any financial institution for the purpose of acquisition of a residential house property.

(2) The deduction under sub-section (1) shall not exceed one lakh rupees and shall be allowed in computing the total income of the individual for the assessment year beginning on the 1st day of April, 2014 and in a case where the interest payable for the previous year relevant to the said assessment year is less than one lakh rupees, the balance amount shall be allowed in the assessment year beginning on the 1st day of April, 2015.

(3) The deduction under sub-section (1) shall be subject to the following conditions, namely:—

- (i) the loan has been sanctioned by the financial institution during the period beginning on the 1st day of April, 2013 and ending on the 31st day of March, 2014;
- (ii) the amount of loan sanctioned for acquisition of the residential house property does not exceed twenty-five lakh rupees;
- (iii) the value of the residential house property does not exceed forty lakh rupees;
- (iv) the assessee does not own any residential house property on the date of sanction of the loan.

(4) Where a deduction under this section is allowed for any interest referred to in sub-section (1), deduction shall not be allowed in respect of such interest under any other provisions of the Act for the same or any other assessment year.

(5) For the purposes of this section,—

- (a) "financial institution" means a banking company to which the Banking Regulation Act, 1949 (10 of 1949) applies including any bank or banking institution referred to in section 51 of that Act or a housing finance company;
- (b) "housing finance company" means a public company formed or registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes.

DONATION FOR SCIENTIFIC RESEARCH/RURAL DEVELOPMENT [SECTION 80GGA]

Deduction is available to any assessee not having business income but making donation to specified institution or fund.

Deduction is equal to the amount donated to specified institution or fund.

Specified Institution or fund:

- (a) Approved Research Association, University, College or other institution to be used for scientific research or social science or statistical research (Section 35);
- (b) Public sector company or a local authority for carrying out any eligible project or scheme (Section 35AC);
- (c) Association or institution approved for the purpose of section 35CCA for undertaking rural development programme or training of persons for implementing programmes of rural development;
- (d) National Urban Poverty Eradication Fund;
- (e) National Fund for Rural Development.

No deduction shall be allowed under this section in respect of any sum exceeding ten thousand rupees unless such sum is paid by any mode other than cash.

CONTRIBUTION TO POLITICAL PARTIES BY AN INDIAN COMPANY [SECTION 80GGB]

100% of contribution to political parties or an electoral trust is allowed as deduction in the hands of an Indian company.

CONTRIBUTION TO POLITICAL PARTIES BY OTHER THAN INDIAN COMPANY [SECTION 80GGC]

In computing the total income of an assessee, being any person, except local authority and every artificial juridical person wholly or partly funded by the Government, there shall be deducted any amount of contribution made in the previous year to a political party or an electoral trust.

Contribution not to be In Cash for Deduction under Section 80GGB & Section 80GGC [Amendment by the Finance Act, 2013]

Under the existing provisions of section 80GGB, any sum contributed by an Indian company to any political party or an electoral trust in the previous year, is allowed as deduction in computing the total income of such Indian company. A similar deduction is available to an assessee, being any person other than local authority and artificial juridical person under section 80GGC. There is no specific mode provided for making such contribution.

With a view to discourage cash payments by the contributors, the provisions of aforesaid sections are amended so as to provide that no deduction shall be allowed under sections 80GGB and 80GGC in respect of any sum contributed by way of cash.

DEDUCTION OF PROFITS FROM BIODEGRADABLE WASTES [SECTION 80JJA]

Deduction is available to any assessee engaged in the business of collecting and processing or treating of biodegradable wastes for generating power or producing bio-fertilizer, bio-pesticides or other biological agents or for producing bio-gas, making pellets or briquettes for fuel or organic manure.

Deduction allowed is 100% of the profits of such business for the initial 5 consecutive Assessment Years from the PYs when the business commences.

DEDUCTION IN RESPECT OF ROYALTY FROM BOOKS [SECTION 80QQB]

Deduction is available to a resident individual who is an author including a joint author who earns royalty from the copyright of books.

Computation of royalty: Where the author receives royalty on yearly basis (not a lump sum consideration in lieu of all rights) in such case, royalty cannot exceed 15% of the value of such books sold during the previous year.

Expenses attributable for earning the royalty income are subtracted from royalty income.

Deduction is equal to an amount equal to lower of royalty income as computed above (brought into India) or ₹3,00,000.

Note:

- (a) Where the income is earned from any source outside India, then the deduction shall be limited to so much of the income which is brought into India in convertible foreign exchange within a period of 6 months from the end of the previous year in which such income is earned or within such further period as the competent authority may allow in this behalf.
- (b) The assessee shall furnish a certificate in the prescribed form, duly signed by the prescribed authority, along with the return of income setting forth such particulars as may be prescribed.

DEDUCTION OF ROYALTY ON PATENTS [SECTION 80RRB]

Deduction is available to a Resident Individual assessee who is a patentee and is in receipt of any income by way of royalty in respect of a patent registered on or after 1.4.2003 under the Patents Act, 1970.

Royalty income excludes any consideration chargeable under the head Capital gains or consideration for sale of product manufactured with the use of patented process or of the patented article for commercial use.

Amount of deduction is equal to lower of the royalty income (brought in India) or ₹ 3,00,000.

Note:

- (a) Where the income is earned from any source outside India, then the deduction shall be limited to so much of the income which is brought into India in convertible foreign exchange within a period of 6 months from the end of the previous year in which such income is earned or within such further period as the competent authority may allow in this behalf.
- (b) The assessee shall furnish a certificate in the prescribed form, duly signed by the prescribed authority, along with the return of income setting forth such particulars as may be prescribed.

OFFSHORE BANKING UNITS [SECTION 80LA]

Deduction is available to a bank located in a Special Economic Zone for 100% of income for 5 consecutive assessment years and 50% of such income for 5 consecutive assessment years.

Assessee need to furnish the report of a Chartered Accountant certifying that the deduction has been correctly claimed.

PROFIT LINKED DEDUCTIONS

Certain common points in relation to profit linked deductions:

- (a) **Eligible business is the only business:** For computing deduction under section 80-IA/80-IB/80-IC/80-ID/80-IE, assume that the eligible business is the only business in the initial assessment year and in subsequent assessment years.
- (b) **Correct profits to be determined by AO if profits of the assessee overstated:** If the assessee overstates the profits of the unit to which deduction under section 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE is available, then Assessing Officer shall take the correct profits to determine the deduction under section 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE. The Chapter of transfer pricing shall be applicable as per Finance Act, 2012.
- (c) **Deduction in case of amalgamation or demerger:** Where an undertaking which is entitled to deduction under section 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE is transferred in the scheme of amalgamation or demerger, then no deduction under section 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE shall be available to the amalgamating or the demerged company for the previous year in which amalgamation or demerger takes place. The provisions of section 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE shall apply to the amalgamated or the resulting company in the same manner in which they would have applied to the amalgamating or the demerged company if the amalgamation or demerger had not taken place.
- (d) **Deductions from GTI:** Deduction under Chapter VI-A i.e. under section 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE and deduction under section 10AA are given from the Gross Total Income (GTI) computed after setting off the brought forward losses and brought forward depreciation.
- (e) **Set off and Carry forward of losses:** If the undertaking to which section 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE or section 10AA applies, suffer a loss, then such loss shall be set off and carried forward.
- (f) **Profit of undertaking not to include Cash compensatory support, duty drawback etc.:** The profits of the undertaking which is deductible under sections 80-IA/80-IB/80-IAB/80-IC/80-ID/80-IE or section 10AA means the profit under the head Profits and gains of business or profession. However, as per Supreme Court in case of Liberty India held that the following shall not form part of the profits of the business of such undertakings:
 - (i) Cash compensatory support (CCS);
 - (ii) Duty drawback;
 - (iii) Profit on sale of import entitlement licenses;
 - (iv) Duty Exemption Pass Book (DEPB).

DEDUCTION NOT TO BE ALLOWED UNLESS RETURN FURNISHED [SECTION 80AC]

Where in computing the total income of an assessee of the previous year relevant to the assessment year commencing on the 1st day of April, 2006 or any subsequent assessment year, any deduction is admissible

under section **80-IA** or section **80-IAB** or section **80-IB** or section **80-IC** or section **80-ID** or section **80-IE**, no such deduction shall be allowed to him unless he furnishes a return of his income for such assessment year on or before the due date specified under sub-section (1) of section 139.

Example: A Ltd. is eligible to claim deduction under Section 80-IA. Due date of filing of return under Section 139(1) in case of A Ltd. is 30th September, 2014 for AY 2014-15. However, return is filed on 1st October, 2014. In this case, as per Section 80AC, deduction under section 80-IA would not be available to company as it has furnished its return of income beyond due date provided under section 139(1).

Therefore, filing of return of income upto due date of filing of return is a pre-requisite for claiming deductions mentioned under section 80AC.

DEDUCTION IN RESPECT OF PROFITS AND GAINS FROM UNDERTAKINGS ENGAGED IN INFRASTRUCTURE DEVELOPMENT, ETC. [SECTION 80-IA]:

(1) Eligible Assessee: This deduction is available to the following assessees:

- (a) Any assessee carrying on the business of (i) developing, or (ii) operating and maintaining or (iii) developing, operating and maintaining any infrastructure facility.

Infrastructure facility means:

- (i) A road including toll road, a bridge or a rail system;

As per CBDT circular no. 4/2010, the widening of an existing road by constructing additional lanes as a part of a highway project by an undertaking would be regarded as a new infrastructure facility for the purposes of section 80-IA. However, simply relaying of an existing road would not be classifiable as a new infrastructure facility for this purpose.

- (ii) A highway project including housing or other activities being an integral part of the highway project;
- (iii) A water supply project, water treatment system, irrigation project, sanitation and sewerage system or solid waste management system.
- (iv) A port, airport, inland waterway or inland port or navigational channel in the sea.

- (b) Any assessee which starts providing telecommunication services whether basic or cellular on or before 31st March, 2005.

- (c) Any assessee which develops, develops and operates and maintain, or maintains and operates a Special Economic Zone (SEZ).

- (d) An assessee which sets up in any part of India, the business of generation or generation and distribution of power upto 31st March, 2014 (**Sunset date for power sector extended from 31st March, 2013 to 31st March, 2014 by Finance Act, 2013**).

2. Period of deduction: The deduction under section 80-IA shall be 100% of the profits and gains derived from the eligible business for a period of 10 consecutive assessment years.

However, in case of telecommunication services, deduction shall be 100% of the profits and gains for the first five assessment years and thereafter 30% of such profits and gains for further five assessment years.

3. Option to avail 10 years deduction out of 15/20 years: The deduction may at the option of the assessee be claimed by him for any 10 consecutive assessment years out of 15 years beginning with the year in which the assessee starts the above business.

However, the option is any 10 consecutive assessment years out of a block of 20 years in case of

an assessee who is covered under 1(a)(i)/(ii)/(iii) above.

- 4. No deduction in a scheme of amalgamation or demerger:** Deduction shall not be allowed under section 80-IA to any undertaking which is transferred in a scheme of amalgamation or demerger.

Note: Nothing contained in section 80-IA shall apply in relation to a business referred to in section 80-IA which is in the nature of a works contract awarded by any person (including the Central or State Government) and executed by the undertaking referred in this section.

DEDUCTION IN RESPECT OF PROFITS AND GAINS FROM CERTAIN INDUSTRIAL UNDERTAKINGS OTHER THAN INFRASTRUCTURE DEVELOPMENT UNDERTAKINGS [SECTION 80-IB]

In case of an assessee whose gross total income includes any profits and gains from any business of an Industrial undertaking, then deduction of following amount shall be allowed to the assessee:

- (a) Deduction for Industrial undertaking in backward areas:** In case an Industrial undertaking is located in an Industrially backward State or industrially backward district (as may be specified by the Central Government in the Official Gazette), deduction will be 100% of the profits and gains derived from such undertaking for initial five assessment years and it will be 25% (30% in case of company assessee) of such profits for subsequent five assessment years.

Conditions: Deduction will be available to an industrial undertaking only if satisfies following conditions:

- **Not formed by splitting:** It is not formed by splitting up, or the reconstruction of a business in existence except in the circumstances and period given in section 33B (Rehabilitation allowance).
- **New plant and machinery:** It is not formed by the transfer to a new business of machinery or plant previously used for any purpose. However, if the new undertaking is started in an old building or if old furniture and fittings are used, then deduction will be available.

Imported plant and machinery: Any machinery or plant which was used outside India by any person other than the assessee shall not be regarded as machinery or plant previously used for any purpose, if the following conditions are fulfilled, namely :—

- (a) such machinery or plant was not, at any time previous to the date of the installation by the assessee, used in India;
- (b) such machinery or plant is imported into India from any country outside India; and
- (c) no deduction on account of depreciation in respect of such machinery or plant has been allowed or is allowable under the provisions of this Act in computing the total income of any person for any period prior to the date of the installation of the machinery or plant by the assessee.

Old plant and machinery: Where in the case of an industrial undertaking, any machinery or plant or any part thereof previously used for any purpose is transferred to a new business and the total value of the machinery or plant or part so transferred does not exceed twenty per cent of the total value of the machinery or plant used in the business, then, the condition shall be deemed to have been complied with.

Deduction in the subsequent year/s in which condition of upto 20% old plant and machinery is satisfied: In the case of **CIT vs. Seeyan Plywoods [190 ITR 564(Ker)]**, Kerala High Court held that if the assessee is not entitled to deduction in the year in which industrial

undertaking is started because the value of old machinery exceeds 20%, the assessee will be eligible to claim deduction in the subsequent years if the value of old plant and machinery does not exceed 20% of the total value of the machinery in the subsequent years.

- **Sunset dates:** It begins to manufacture or produce articles or things at any time upto 31st March, 2004 and in case of Jammu and Kashmir, upto 31st March, 2012.
 - The undertaking employs ten or more workers in a manufacturing process carried on with the aid of power or employs twenty or more workers in a manufacturing process carried on without the aid of power.
- (b) **Deduction to undertaking beginning commercial production or refining of mineral oil in India:** In this case, undertaking would be allowed a deduction of 100% of the profits and gains from such business for the initial 7 assessment years beginning from the assessment year relevant to previous year in which the commercial production or refining of mineral oil is started.
- (c) **Deduction to undertaking engaged in commercial production of natural gas in blocks licensed under the New Exploration Licensing Policy (NELP-VIII):** In this case, undertaking would be allowed a deduction of 100% of the profits from such undertaking for a period of 7 consecutive assessment years beginning from the assessment year relevant to previous year in which the undertaking commences commercial production of natural gas.
- (d) The amount of deduction in the case of an undertaking developing and building housing projects approved by a local authority shall be 100% of the profits derived in any previous year from such housing project if:
- (i) Such undertaking commences development and construction of the housing project and completes such construction within 5 years from the end of the financial year in which the housing project is approved by the local authority;
 - (ii) The project is on the size of a plot of land which has a minimum area of one acre;
 - (iii) The built up area of the shops and other commercial establishments included in the housing project does not exceed 3% of the aggregate built up area of the housing project or five thousand square feet, whichever is higher.
 - (iv) Not more than one residential unit in the housing project is allotted to any person being an individual; and
 - (v) In a case where a residential unit in the housing project is allotted to a person being individual, no other residential unit in such housing project is allotted to any of the following persons, namely:
 - The individual or the spouse or the minor children of such individual;
 - The HUF in which such individual is the Karta;
 - Any person representing such individual, the spouse or the minor children of the individual or the HUF in which such individual is the Karta.

Note: Nothing contained in this sub-section shall apply to any undertaking which executes the housing project as a works contract awarded by any person (including the Central or State Government).

Amount and period of deduction: The deduction is 100% of the profits derived from the housing project in any previous year. Therefore, deduction would be allowed for the period during which houses are sold and profit is earned.

As per CBDT circular, deduction can be claimed on a year to year basis where assessee is

showing profit from partial completion of project. If later any of the condition is violated, then deduction allowed in earlier years shall be withdrawn.

- (e) **Profits from business of operating and maintaining a hospital:** The amount of deduction in the case of an undertaking deriving profits from the business of operating and maintaining a hospital located anywhere in India, other than the excluded area, shall be 100% of the profits and gains derived from such business for a period of 5 consecutive assessment years beginning with the initial assessment year, if the hospital has at least 100 beds for patients and the construction of the hospital is in accordance with the regulations or bye-laws of the local authority.

SPECIAL PROVISIONS IN RESPECT OF CERTAIN UNDERTAKINGS IN CERTAIN SPECIAL CATEGORY STATES [SECTION 80-IC]

The deduction is available to an assessee whose gross total income includes any profits and gains derived from:

- (a) Any undertaking which manufactures or produces any article or thing, and undertakes substantial expansion in the state of Himachal Pradesh or Uttranchal on or before 31st March, 2012.
Substantial expansion for above purpose, means increase in the investment in the plant and machinery by at least 50% of the book value of plant and machinery (before taking depreciation in any year), as on the first day of the previous year in which the substantial expansion is undertaken.
- (b) Any undertaking which has begun or begins to manufacture or produce any article or thing in Himachal Pradesh or Uttranchal on or before 31st March, 2012.

The deduction under section 80-IC shall be 100% of the profits and gains of the Industrial undertaking for the first 5 years commencing from the initial assessment year and 25% (30% in the case of a company) for the next 5 years.

Initial assessment year means the assessment year relevant to the previous year in which the undertaking begins to manufacture or produce articles or things, or completes substantial expansion.

DEDUCTION IN RESPECT OF PROFITS AND GAINS FROM BUSINESS OF HOTELS [SECTION 80-ID]

A deduction of an amount equal to 100% of the profits and gains from the business of hotel (of two star or above category) located in the specified district having a World Heritage Site shall be allowed to the assessee for 5 consecutive assessment years beginning from the initial assessment year.

SPECIAL PROVISIONS IN RESPECT OF CERTAIN UNDERTAKINGS IN NORTH EASTERN STATES (SECTION 80-IE)

A deduction of 100% of the profits and gains for 10 consecutive assessment years shall be allowed to an assessee which (a) begins to manufacture or produce any eligible article or thing; or (b) undertake substantial expansion to manufacture or produce any eligible article or thing; or (c) carry on any eligible business, in North Eastern State.

Notes:

- (a) **Meaning of substantial expansion:** It means increase in the investment in the plant and machinery by at least twenty five percent of the book value of the plant and machinery (before taking depreciation in any year), as on the first day of the previous year in which the substantial expansion is undertaken.
- (b) **Eligible article or thing:** It means the article or thing other than (i) goods which pertains to tobacco

and manufactured tobacco substitutes; (ii) pan masala; (iii) plastic carry bags.

(c) **Eligible business:** It means the business of :

- (i) Hotel (not below two star category);
- (ii) Adventure and leisure sports including ropeways;
- (iii) Providing medical and health services in the nature of nursing home with a minimum capacity of 25 beds;
- (iv) Running an old-age home;
- (v) Operating vocational training institute for hotel management, catering and food craft, entrepreneurship development, nursing and para-medical, civil aviation related training, fashion designing and industrial training;
- (vi) Running information technology related training centre;
- (vii) Manufacturing of information technology hardware; and
- (viii) Bio-technology.

DEDUCTION IN RESPECT OF INTEREST ON DEPOSITS IN SAVINGS ACCOUNT (SECTION 80TTA)

(1) Where the gross total income of an assessee, being an individual or a Hindu undivided family, includes any income by way of interest on deposits (not being time deposits) in a savings account with –

- (a) a banking company to which the Banking Regulation Act, 1949 (10 of 1949), applies (including any bank or banking institution referred to in section 51 of that Act);
- (b) a co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank); or
- (c) a Post Office as defined in clause (k) of section 2 of the Indian Post Office Act, 1898 (6 of 1898), there shall be allowed in computing the total income of the assessee, a deduction which shall not exceed Rs.10,000.

(2) Where the income referred to in this section is derived from any deposit in a savings account held by, or on behalf of, a firm, an association of persons or a body of individuals, no deduction shall be allowed under this section in respect of such income in computing the total income of any partner of the firm or any member of the association or any individual of the body.

"Time deposits" means the deposits repayable on expiry of fixed periods.

SPECIAL PROVISION IN RESPECT OF NEWLY ESTABLISHED UNITS IN SPECIAL ECONOMIC ZONES [SECTION 10AA]

- (1) In computing the total income of an undertaking, which begins to manufacture or produce articles or things or computer software in any Special Economic Zone (SEZ), the deduction shall be:
 - (a) 100% of export profits for first five assessment years;
 - (b) 50% of export profits for next five assessment years;
 - (c) Amount debited to Profit and Loss Account and credited to SEZ Reinvestment Allowance Reserve A/c subject to a maximum of 50% of export profits, for next five assessment years.
- (2) Export profits shall be computed as under:

Export profits = Profits of the business of the undertaking to which Section 10AA applies (as

computed under the head PGBP) \times Export turnover of the Undertaking to which section 10AA applies/Total turnover of the Undertaking to which section 10AA applies.

Export Turnover: It means the consideration in respect of export received in, or brought into India by the assessee in convertible foreign exchange, within a period of six months from the end of the previous year period as may be permitted by the RBI, but does not include freight, telecommunication charges or insurance attributable to the delivery of the articles or things or computer software outside India or expenses, if any, incurred in foreign exchange in providing the technical services outside India.

Note: The sale proceeds referred to above shall be deemed to have been received in India where such sale proceeds are credited to a separate account maintained for the purpose by the assessee with any bank outside India with the approval of the Reserve Bank of India.

- (3) Section 10AA is a deduction and therefore, losses and depreciation of undertaking to which section 10AA applies shall be carried forward normally.

SELF TEST QUESTIONS

(These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.)

1. Determine the residential status of T in the following cases, for the Assessment Year 2014-15:
 - (a) T comes to India and stays from 9th June, 2013 to 18th November, 2013. She never came to India before that.
 - (b) T is an Indian citizen and is a crew member of an Indian ship. She stays in India during the relevant year as follows: 1st April to 27th June, 2013 and then thereafter, 18th February, 2013 for another 180 days.
 - (c) T comes to India in every year for 99 days. She is doing the same from last 10 years. Will your answer change if she comes to India in every year for 108 days.
 - (d) T is an Indian citizen and she comes to India for joining a job of Company Secretary in an Indian company on 9th January, 2013. She stayed the entire financial year 2011-12 in India. Prior to this, she never came to India.
 - (e) T has never gone out of India prior to leaving India on 18th June, 2013.
 - (f) T, a U.S. citizen was born in 1935 in Delhi. She comes on a vacation to India as a part of her world tour on 18th January, 2014 and stays in India for 234 days.
2. TA & Co. (HUF) is registered in India and all its decisions are taken outside India. Determine residential status of HUF for AY 2014-15 assuming Karta of HUF is (a) ROR in India; (b) RNOR in India and (c) Non-Resident in India.
3. How would you deal with the following in computing taxable profits from business or profession:
 - (i) Foreign Travel expenses incurred to purchase machinery for factory.
 - (ii) Theft of stock in trade when it was not insured.
 - (iii) Legal charges incurred for framing the scheme of amalgamation of D company with the assessee company.
 - (iv) Consultation fees paid to tax advisor.
 - (v) Voluntary payment of gratuity paid on account of commercial expediency to an employee who died on business tour.

4. Mrs. Radhika provides the following details of her financial transactions during the year 2013-14:

- (i) She received Rs. 63,000 interest on securities of Central Government.
- (ii) She received Rs. 48,000 interest from non-listed debentures of XYZ Ltd.
- (iii) She received a gift of agricultural land, having stamp duty value of Rs. 40,000.
- (iv) She received money gifts from funds, aggregating Rs. 1,50,000 on her marriage anniversary.
- (v) She got a gift of diamond ring value Rs. 45,000 from a friend on her birthday.

You are requested to determine her total income for the assessment year 2014-15.

Answer/Hints:

1. (a) NR; (b) NR; (c) RNOR if comes for 99 days and ROR if comes for 108 days; (d) RNOR; (e) ROR; (f) NR
2. NR in all the cases.

SUGGESTED READINGS

- | | | |
|------------------------------|---|--|
| 1. Girish Ahuja & Ravi Gupta | : | Professional Approach to Direct Taxes-Law and Practice |
| 2. Dr. V K Singhania | : | Direct Taxes Law and Practices |
| 3. B.B. Lal and N. Vashist | : | Direct Taxes, Income Tax, Wealth Tax and Tax Planning |

TAXATION OF INDIVIDUALS, PARTNERSHIP FIRMS/LLP AND COMPANIES

PART II: TAXATION OF PARTNERSHIP FIRMS/LIMITED LIABILITY PARTNERSHIP

After completing this part, a student will:

- Understand assessment of Partnership Firm or LLP,
- Be familiar with the deduction of interest and partner's salary to partners,
- Know the concept of Alternate Minimum Tax (AMT)

ASSESSMENT AS A FIRM [SECTION 184]

A firm shall be assessed as a firm for the purposes of the Act if:

- (a) The partnership is evidenced by an instrument; and
- (b) The individual shares of the partners are specified in the instrument;
- (c) A certified copy of the instrument of partnership referred above should accompany the return of income of the previous year relevant to assessment year in respect of which assessment as a firm is first sought;

The copy of partnership deed shall be certified in writing by all the partners (not being minors), or, where the return is made after dissolution of the firm, by all persons who were partners in the firm immediately before its dissolution and by the legal representative of any such partner who is deceased.

Where the firm is assessed as such for any assessment year, it shall be assessed in the same capacity for every subsequent year if there is no change in the constitution of the firm or the shares of the partners as evidenced by the partnership deed on the basis of which the assessment as a firm was first sought.

Where any change in constitution takes place in the previous year, the firm shall furnish a certified copy of the revised partnership deed along with the return of income for the assessment year relevant to such previous year.

If the firm does not comply with the conditions of section 184 or there is any failure on the part of the firm as is mentioned in section 144 of the Act, then the interest and remuneration paid to partners (even if conditions of section 40(b) are satisfied) will be fully disallowed in the hands of the firm. Such interest and remuneration, then, shall not be taxable under section 28(v) in the hands of partners.

PAYMENT OF INTEREST, SALARY, BONUS, COMMISSION OR REMUNERATION MADE BY FIRM TO ITS PARTNERS [SECTION 40(b)]

Interest and remuneration paid to partners by a firm are allowed as deduction to the firm if following conditions are satisfied:

- (a) **Payment to a working partner:** Payment of salary, bonus, commission or remuneration must be to a working partner as these payments to a non-working partners are disallowed.
- (b) **Partnership deed to contain provision for remuneration:** Remuneration shall be admissible only if the partnership deed either specifies the amount of remuneration payable to each working partner or lays down the manner of quantifying such remuneration.
- (c) **Payment after date of partnership deed:** Partnership deed should not provide for payment of remuneration and interest from retrospective effect.

(d) Interest upto 12% p.a. is allowed: Payment of interest to a partner should be upto 12% per annum simple interest. Excess, if any, to partners will be disallowed for the firm.

If a firm pays interest to a partner and the partner pays interest to the firm on his drawings, then the interest shall not be netted off. The interest received by the firm from the partners on their drawings is taxable in the hands of the firm as its business or professional income. The interest paid by the firm to the partners is allowable as per section 40(b).

Interest paid by the firm to its partners on their fixed capital account, current capital account and loan account is allowable as deduction to the firm provided the partnership deed specifically authorises the payment of interest on fixed capital account, current capital account and loan account. If the partnership deed authorises the payment of interest on fixed capital account, then interest on current capital account and loan account shall not be allowed as deduction to the firm.

(e) Payment of remuneration to working partners: It is subject to maximum of the following limits and amount paid in excess of the limit below is disallowed to the firm:

Book Profit	% age of book profit
On the first ₹ 3,00,000 of the book-profit or in case of a loss	₹ 1,50,000 or 90% of the book-profit, whichever is more.
On the balance of the book profit	60% of the book profit.

MEANING OF BOOK PROFIT [EXPLANATION 3 TO SECTION 40(B)]

Book profit means the net profit, as shown in the profit and loss account and after making the additions and deductions as per section 28 to 44D of the Act and increased by the total remuneration paid or payable to all the partners of the firm if such amount has been deducted while computing the net profit. Interest paid/payable to partners in excess of 12% shall also be disallowed as per section 40(b).

Note:

Explanation 1 to section 40(b): Where an individual is a partner in a firm in a representative capacity, then interest paid by the firm to him in individual capacity, shall not be taken into account for the purposes of section 40(b).

Explanation 2 to section 40(b): Where an individual is a partner in a firm in his individual capacity then, interest paid by the firm to such individual shall not be taken into account for the purposes of section 40(b), if such interest is received by him on behalf, or for the benefit of any other person.

Salary paid to partner representing his HUF has to be disallowed. Further, salary paid to partners in their individual capacity who had joined firm as partners representing their respective HUFs is also to be disallowed.

TAXATION OF FIRM AND ITS PARTNERS

Income of the partnership firm is assessed at a flat rate of tax i.e. 30% plus applicable surcharge and education cess & secondary and higher education cess.

Shares of partners in the total (taxable) income of the firm is exempt in the hands of partners under section 10(2A). Losses of the firm shall be carried forward by a firm shall not be allocated to the partners.

Remuneration and interest paid to the partners is allowed as deduction to the firm subject to the limits and conditions specified in section 40(b). Such remuneration and interest received by the partners shall be taxed in their hands as business/profession income under section 28(v). However, salaries and interest disallowed

under section 40(b) or section 184(5) or section 185 shall not be added to the income of the partners under section 28(v).

CARRY FORWARD AND SET OFF OF LOSSES

The losses and unabsorbed depreciation of firm can be carried forward by it only. Section 78(1) provides that where a change in constitution of firm takes place on account of retirement of partner or death of the partner, then, the firm shall not carry forward and set off the brought forward losses to extent of following:

Share of the retired/deceased partner in the brought forward losses of the firm **minus** share of the retired/deceased partner in the current year profit.

However, section 78(1) does not apply to unabsorbed depreciation which shall be carried forward by the firm even if a partner retires or dies.

Section 78(1) does not apply if change in constitution takes place on admission of a new partner or if all partner remain with a change in profit sharing ratio.

IMPACT OF CHANGE IN THE CONSTITUTION OF FIRM

There is a change in the constitution of the firm if one or more partners cease to be partners or one or more new partners are admitted, in such circumstances that one or more of the persons who were partners of the firm before the change, continue as partner or partners after the change. However, nothing mentioned above will apply if firm is dissolved on the death of any of its partners.

Further, there is a change in constitution of firm where all the partners continue with a change in the respective shares or in the shares of some of them.

Where at the time of making an assessment under section 143, section 144 or section 147 or section 153A, it is found that a change has occurred in the constitution of a firm, the assessment shall be made on the firm as constituted at the time of making the assessment.

SUCCESSION OF ONE FIRM BY ANOTHER FIRM [SECTION 188]

Where a firm carrying on a business or profession is succeeded by another firm, and the case is not the one covered by section 187, separate assessment shall be made on the predecessor firm (upto the date of succession) and on the successor firm (after the date of succession).

JOINT AND SEVERAL LIABILITY OF PARTNERS FOR TAX PAYABLE BY FIRM [SECTION 188A]

Every person who was, during the previous year, a partner of a firm, and the legal representative of any deceased partner, shall be jointly and severally liable along with the firm for the amount of tax, penalty or other sum payable by the firm for the assessment year to which such previous year is relevant.

ASSESSMENT OF FIRM DISSOLVED OR BUSINESS DISCONTINUED [SECTION 189]

If a firm has been dissolved or business discontinued, the AO shall make an assessment of the total income of the firm as if no such discontinuance or dissolution had taken place. All the provisions of the Income-tax Act including provisions relating to the levy of penalty shall apply to such assessment.

Every person who was at the time of such discontinuance or dissolution a partner of the firm, and the legal representative of any such person who is deceased, shall be jointly and severally liable for the amount of tax, penalty or any other sum payable under the Act for all the assessment years since the formation of the firm. Where such discontinuance or dissolution takes place after any proceedings in respect of an assessment

year have commenced, the proceedings may be discontinued against the legal representative from the stage at which the proceeding stood at the time of such discontinuance or dissolution and all the provisions of the Income-tax act shall apply.

TAXATION OF LIMITED LIABILITY PARTNERSHIP (LLP)

The concept of LLP came in India with the introduction of the Limited Liability Partnership Act 2008.

LLP shall have the same status as that of partnership firms formed under the Indian Partnership Act, 1932 for the purposes of Income tax. The definition of firm, partner and partnership has been amended to include the LLP within its purview.

As per Section 2(23) of the Income-tax Act, 1961:

- (a) "firm" shall have the meaning assigned to it in the Indian Partnership Act, 1932, and shall include a limited liability partnership as defined in the Limited Liability Partnership Act, 2008;
- (b) "partner" shall have the meaning assigned to it in the Indian Partnership Act, 1932 and shall include any person who, being a minor has been admitted to the benefits of partnership; and a partner of a limited liability partnership as defined in the Limited liability Partnership Act, 2008.
- (c) "partnership" shall have the meaning assigned to it in the Indian Partnership Act, 1932, and shall include a limited liability partnership as defined in the Limited Liability Partnership Act, 2008.

There will be no implication under the Income-tax Act where a partnership firm is converted into a LLP.

As per Finance Act, 2011, Capital gains shall be exempt when a company is converted into a LLP.

Under Section 140, Return of Income shall be signed by designated partner or where designated partner is not able to sign due to unavoidable reasons, any partner shall sign Return of Income.

As per Section 167C of the Act, the liability of the partners of LLP shall be joint and several for the payment of such tax unless he proves that the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the limited liability partnership.

Alternate Minimum Tax (AMT) on all persons other than companies

From the assessment year 2012-13 onwards, where the regular income tax payable for a previous year by a limited liability partnership is less than the alternate minimum tax payable for such previous year then the adjusted total income shall be deemed to be the total income of the LLP for such previous year and it shall be liable to pay income tax on such adjusted total income @ **18.5% plus education & SHEC @ 3%**.

Upto Assessment Year 2012-13, Alternate Minimum Tax (AMT) is levied on limited liability partnerships (LLPs). However, no such tax is levied on the other form of business organisations such as partnership firms, sole proprietorship, association of persons, etc.

In order to widen the tax base vis-à-vis profit linked deductions, the provisions regarding AMT has been broaden to cover all persons other than a company, who has claimed deduction under any section (other than section 80P) included in Chapter VI-A under the heading "C – Deductions in respect of certain incomes" or under section 10AA, shall be liable to pay AMT.

Accordingly, where the regular income-tax payable for a previous year by a person (other than a company) is less than the alternate minimum tax payable for such previous year, the adjusted total income shall be deemed to be the total income of such person and he shall be liable to pay income-tax on such total income at the rate of **eighteen and one-half per cent**.

For the purpose of the above,

- (i) "adjusted total income" shall be the total income before giving effect to provisions of Chapter XII-BA as increased by the deductions claimed under any section (other than section 80P) included in Chapter VI-A under the heading "C – Deductions in respect of certain incomes" and deduction claimed under section 10AA;
- (ii) "alternate minimum tax" shall be the amount of tax computed on adjusted total income at a rate of eighteen and one half cent; and
- (iii) "regular income-tax" shall be the income-tax payable for a previous year by a person other than a company on his total income in accordance with the provisions of the Act other than the provisions of Chapter XII-BA.

It is further provided that the provisions of AMT under Chapter XII-BA shall not apply to an individual or a Hindu undivided family or an association of persons or a body of individuals (whether incorporated or not) or an artificial juridical person referred to in section 2(31)(vii) if the adjusted total income of such person **does not exceed twenty lakh rupees**.

It is also provided that the credit for tax (tax credit) paid by a person on account of AMT under Chapter XII-BA shall be allowed to the extent of the excess of the AMT paid over the regular income-tax. This tax credit shall be allowed to be carried forward up to the tenth assessment year immediately succeeding the assessment year for which such credit becomes allowable. It shall be allowed to be set off for an assessment year in which the regular income-tax exceeds the AMT to the extent of the excess of the regular income-tax over the AMT.

Every person to which this section applies shall obtain a report, in such form as may be prescribed from an accountant certifying that the adjusted total income and the alternate minimum tax have been computed in accordance with the provisions of this Chapter and furnish such report on or before the due date of filing of return under sub-section (1) of section 139.

Illustration

X and Y are two partners (1:2) of X Co., a firm engaged in manufacturing chemicals. The profit and loss account of the firm for the year ending 31.3.2014 is as follows:

Particulars	Amount (₹)	Particulars	Amount (₹)
Cost of goods sold	86,00,000	Sales	1,26,00,000
Salary to staff	17,79,600	Long term capital gains	80,000
Depreciation	1,60,000	Other business receipts	62,000
<i>Remuneration to partners:</i>			
X	6,00,000		
Y	4,80,000		
<i>Interest on capital to partners @</i>			
18%			
X	72,000		
Y	50,400		
<i>Other expenses</i>	7,40,000		
<i>Net Profit</i>	2,60,000		
	<u>1,27,42,000</u>		<u>1,27,42,000</u>

Other information:

- (1) The firm completed all legal formalities to get the status of 'Firm'.
- (2) The firm has given donation of ₹ 1,60,000 to a notified public charitable trust which is included in other expenses.
- (3) Salary and interest is paid to partners as per the partnership deed.
- (4) Depreciation allowable under section 32 is ₹ 1,56,000.
- (5) Income and investment of X and Y are as follows:

	X (₹)	Y (₹)
Interest on company deposit	1,28,000	1,01,600
Dividend from foreign companies	14,000	22,000
Long term capital gains (loss)	1,60,000	40,000
Short term capital gains (loss)	6,000	(12,000)
Winning from lotteries (Gross)	8,000	20,000
Contribution towards Home Loan A/c of National Housing Bank	80,000	1,20,000

Find out the Net Income and tax liability of the firm and partners for the Assessment Year 2014-15.

Solution**Computation of Total Income of the Firm for the Assessment Year 2014-15 (Previous Year 2013-14)**

	₹	₹
Net Profit as per Profit and Loss Account		2,60,000
Add: Inadmissible expenses if debited to Profit and Loss Account:		
– Donations to Public charitable trust	1,60,000	
– Interest on capital in excess of 12%:		
X (72,000/18 × 6)	24,000	
Y (50,400/18 × 6)	16,800	
– Remuneration to partners as per Profit and loss account:		
X	6,00,000	
Y	4,80,000	12,80,000
Less: Admissible expenses if not debited to Profit and Loss account		Nil
Less: Incomes taxable under any other head/exempt incomes, if credited to profit and loss account		
– Long term capital gains	(80,000)	(80,000)
Add: Incomes taxable as business income, if not credited to Profit and loss account	Nil	Nil
Total		14,60,000
Add: Depreciation as per Profit and Loss Account		<u>1,60,000</u>
Less: Depreciation as per Income-tax Act		(1,56,000)
Book Profits of Firm		14,64,000
Less: Remuneration allowed to partners:		
Lower of Actual remuneration (6,00,000 + 4,80,000) or Remuneration based on book profits:	10,80,000	
(90% of first ₹ 3,00,000 + 60% of balance 11,64,000)	<u>9,68,400</u>	(9,68,400)
Business Income of the firm		4,95,600
– Long term capital gains		80,000
Gross Total Income		5,75,600

Less: Deductions under section 80C to 80U:

Lower of

– 50% of donation to charitable trust ($1,60,000 \times 50\%$)	80,000
– 50% of eligible amount [10% of Adjusted total income (GTI 5,75,600 – LTCG 80,000) : 49,560]	<u>24,780</u> <u>(24,780)</u>
Total Income of the firm	<u>5,50,820</u>

Tax Liability of the firm:

	₹	₹
Tax on:		
– Long term capital gains of ₹ 80,000 @ 20%	16,000	
– Other Income of ₹ 4,70,820 @ 30%	<u>1,41,246</u>	<u>1,57,246</u>
<i>Add: Surcharge, if any</i>		Nil
<i>Add: Education cess @ 2%</i>		3,145
<i>Add: Secondary and Higher education cess @ 1%</i>		<u>1,572</u>
Tax Liability		1,61,963
Tax liability (rounded off)		<u>1,61,960</u>

Total Income of X and Y:

	<i>X (₹)</i>	<i>Y (₹)</i>
Income from business		
Remuneration from firm (in ratio of actual remuneration i.e. 5:4)	5,38,000	4,30,400
Interest from the firm to the extent allowed as deduction	48,000	33,600
Share of profit (exempt)	–	–
<i>Capital gains:</i>		
– Long term capital gains (loss)	1,60,000	40,000
– Short term capital gains (loss)	6,000	(12,000)
<i>Income from other sources:</i>		
– Interest on company deposits	1,28,000	1,01,600
– Dividend from foreign companies	14,000	22,000
– Winning from lotteries (fully taxable)	<u>8,000</u>	<u>20,000</u>
Gross Total Income	9,02,000	6,35,600
Less: Deduction under section 80C (restricted to ₹ 1,00,000)	<u>(80,000)</u>	<u>(1,00,000)</u>
Total Income	<u>8,22,000</u>	<u>5,35,600</u>

Tax Liability of X and Y:

	<i>X (₹)</i>	<i>Y (₹)</i>
Tax on Long term capital gain @ 20% [$1,60,000 \times 20\%$; 28,000 $\times 20\%$]	32,000	5,600
Tax on lottery income @ 30%	2,400	6,000
Tax on other income:		
– X [20% of (6,54,000-5,00,000) + ₹ 30,000]	60,800	
– Y [10% of (4,87,600-2,00,000)]	<u>—</u>	<u>28,760</u>
Total Tax	<u>95,200</u>	<u>40,360</u>
<i>Add: Surcharge, if any</i>	Nil	Nil

Add: Education cess @ 2%	1,904	807
Add: Secondary and Higher education cess @ 1%	952	404
Total Tax Liability	98,056	41,571
Tax Liability (rounded off)	98,060	41,570

Illustration

AB and Co. is a partnership firm. It has two partners A and B (1:2). The firm is engaged in the business of civil construction including repairs of dams and supply of labour for civil construction. The partnership firm has been assessed as a firm for the assessment year 2014-15. The profit and loss account of the firm for the year ended 31.3.2014 is as follows:

	₹
Opening stock of raw material	31,700
Depreciation	2,39,430
Salary to employees	1,30,000
Purchase of raw material	22,60,210
Interest on loan taken to make deposit in companies	13,800
Interest on loan taken for business purposes	71,400
Travelling, entertainment and advertisement expenses	47,800
Other expenses	3,82,000
Municipal tax and insurance (6000 + 1200) of godown	7,200
Salary to partners as per partnership deed:	
– A	1,08,000
– B	72,000
Interest to partners as per partnership deed @ 24% p.a.	
– A	12,000
– B	60,000
Net Profit	<u>6,94,760</u>
Total	41,30,300
Receipts from the business of civil construction	36,90,700
Rent of a godown	48,000
Interest on company deposits	2,60,000
Closing stock of raw material	<u>1,31,600</u>
Total	41,30,300

Other information:

- (i) Out of other expenses debited to profit and loss account, ₹ 12,700 are not deductible under section 37(1);
- (ii) Out of travelling, advertisement and entertainment expenses, ₹ 17,500 are not deductible under section 37(1);
- (iii) On 1.4.2013, the firm owns the following depreciable assets:

Block 1 – Plants A, B and C depreciated value: ₹ 3,70,000; rate of depreciation : 15%

Block 2 – Plants D and E, depreciated value : ₹ 1,98,000; rate of depreciation : 30%.

On 1.1.2014, the firm sells Plant D for ₹ 6,10,000 and purchases Plant F (rate of depreciation 15%) for ₹ 4,86,000.

- (iv) The firm gives a donation of ₹ 1,70,000 to a notified charitable institute which is included in other expenses.
- (v) The firm wants to set off the following losses brought forward from earlier years:

Particulars	Assessment Years	
	2012-13 (₹)	2013-14 (₹)
Business loss	20,000	Nil
Capital loss	2,000	1,000

- (vi) Income of partners A and B is as follows:

Particulars	A (₹)	B (₹)
Bank Interest	91,000	1,33,000
PPF contribution	10,000	15,000

Find out the net income and tax liability of the firm and partners for the Assessment Year 2014-15.

Solution

Computation of Total Income of the Firm for the Assessment Year 2014-15 (Previous Year 2013-14)

	₹	₹
Income under the head PGBP:		
Income from the business of civil construction (8% of 36,90,700)	2,95,256	
Less: Interest on capital to partners @ 12%	<u>(36,000)</u>	
Book profits	2,59,256	
Less: Remuneration to partners (i.e. lower of ₹ 1,80,000 or 90% of 2,59,256)	<u>(1,80,000)</u>	
Business Income	79,256	
Less: Brought forward business loss of the AY 2012-13	<u>(20,000)</u>	59,256
Income from house property:		
Actual Rent (GAV)	48,000	
Less: Municipal taxes paid	<u>(6,000)</u>	
Net annual value (NAV)	42,000	
Less: Deductions under section 24		
Standard deduction @ 30% of NAV	<u>(12,600)</u>	29,400
Short term capital gain on sale of Plant D (Section 50)		
₹ 6,10,000 – ₹ 1,98,000]	4,12,000	
Less: Brought forward capital loss	<u>(3,000)</u>	4,09,000
Income from other sources:		
Interest on company deposits [2,60,000 – 13,800]	<u>2,46,200</u>	<u>2,46,200</u>
Gross Total Income (GTI)		7,43,856
Less: Deduction under section 80G [50% of (10% of ₹ 7,43,856)]		<u>(37,193)</u>
Total Income (rounded off)		7,06,660

Tax Liability of the firm:

	₹
Tax on Total Income of @ 30%	2,11,998
<i>Add: Surcharge, if any</i>	Nil
<i>Add: Cess @ 3% (Education cess @ 2% and SHEC @ 1%)</i>	<u>6,360</u>
Tax Liability	2,18,358
Tax liability (rounded off)	2,18,360

Total Income of A and B:

	X (₹)	Y (₹)
<i>Income from business</i>		
Remuneration from firm (in ratio of actual remuneration)	1,08,000	72,000
Interest from the firm to the extent allowed as deduction	6,000	30,000
Share of profit (exempt)	—	—
<i>Income from other sources:</i>		
Bank Interest	<u>91,000</u>	<u>1,33,000</u>
Gross Total Income	2,05,000	2,35,000
Less: Deduction under section 80C (restricted to ₹ 1,00,000)	<u>(10,000)</u>	<u>(15,000)</u>
Total Income	<u>1,95,000</u>	<u>2,20,000</u>

Tax Liability of X and Y:

	X (₹)	Y (₹)
Tax liability (rounded off) (as there would be no tax on income upto ₹ 2,20,000 for AY 2014-15)	Nil	Nil

Illustration

Following information is provided of an assessee for the Previous Year 2013-14:

Net profit as per P&L A/c	:	₹ 90,63,000
Depreciation as per P&L A/c	:	₹ 6,20,000
Depreciation as per Income Tax Rules	:	₹ 7,50,000
Inadmissible expenses	:	₹ 1,64,000
Deduction u/s 10AA (computed)	:	₹ 82,70,000
LTCG (on Jewellery)	:	₹ 1,80,000
Deduction under Chapter VIA		
– 80GGC	:	₹ 32,000
– 80-IA	:	₹ 60,200

Compute Total income and Tax liability assuming the assessee is an

- (a) Individual
- (b) HUF
- (c) Firm
- (d) LLP
- (e) AOP
- (f) BOI

Solution

Statement showing computation of Total Income (Applicable for all assesses)

Net Profit as per Profit & Loss A/c	₹ 90,63,000
<i>Add: Inadmissible expenses</i>	1,64,000
<i>Add: Depreciation as per P&L A/c</i>	6,20,000
<i>Less: Depreciation as per Income Tax Rules</i>	(7,50,000)
Total	₹ 90,97,000
<i>Less: Deduction u/s 10AA</i>	(82,70,000)
Business Income	₹ 8,27,000
Long term capital gains	1,80,000
Gross Total Income	₹ 10,07,000
<i>Less: Deduction under chapter VI-A</i>	
– Section 80GGC	(32,000)
– Section 80-IA	(60,200)
Total Income	₹ 9,14,800

Computation of Adjusted Total Income for the purposes of Alternate Minimum Tax

Total Income	₹ 9,14,800
<i>Add: Deduction u/s 10AA</i>	82,70,000
<i>Add: Deduction under Section 80IA</i>	<u>60,200</u>
Adjusted Total Income	₹ 92,45,000

TAX LIABILITY FOR A.Y. 2014-15:

Firm/LLP

(I) Firm/LLP

Tax on:

– LTCG @ 20% (1,80,000 x 20%)	36,000
– Balance Total Income @30% (9,14,800 – 1,80,000)	<u>2,20,440</u>
Tax	2,56,440
<i>Add: Education Cess @ 3%</i>	<u>7,693</u>
Tax Liability (Rounded off)	2.64.130

Tax on Adjusted Income (including cess) @
[18.5% + 3% cess = 19.055% of ATI] (rounded off)

Alternate Minimum Tax (AMT) = Rs. 17,61,630

Tax Payable = Rs. 17,61,630

AMT Credit = $17.61.630 - 2.64.130$

= Rs. 14.97.500

(II) Tax Liability for Individual/HUF/AOP/BOI)

Tax on:	₹	
– LTCG @ 20% $(1,80,000 \times 20\%)$		36,000
– Balance Total Income @ Slab Rate [(7,34,800 – 5,00,000) $\times 20\% + 30,000]$		76,960

Total Tax		1,12,960

Add: Education cess & SHBC @ 3%	3,389
Tax including cess (A)	<u>1,16,350</u>
AMT @ 19.055% of ₹ 92,45,000 (B)	<u>17,61,630</u>

Tax Payable = Higher of (A) and (B)
= ₹ 17,61,630 (Rounded off)
Tax Credit (AMT Credit) = 17,61,630 – 1,16,350
= ₹ 16,45,280

SELF TEST QUESTIONS

(These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.)

1. AT, a limited liability partnership (LLP) is a firm of Company secretaries. It carries out its professional activities in India as well as outside India. All its decisions are taken from India except few decisions which are taken outside India. Determine residential status of LLP for the AY 2014-15.
2. Discuss the provisions for taxability of firm?
3. Explain in brief the condition for allowability of deduction of interest to a partner.
4. Compute the taxable income for assessment year 2014-15 of a partnership firm engaged in retail trade from the following particulars:
 - (i) Net profit of ₹ 3,65,000 arrived at after debit of interest on capital of partners of ₹ 1,80,000 and salaries to working partners of ₹ 4,80,000.
 - (ii) Total capital of the partners on which interest paid is debited in the profit and loss account was ₹ 10,00,000.
5. X, Y and Z are three partners in a firm of lawyers having an equal share in profits. For the assessment year 2014-15 income of the firm from profession is ₹ 40,000 after paying salary of ₹ 72,000 to X and ₹ 48,000 to Y. The interest income of the firm is ₹ 60,000. The personal incomes of X, Y and Z are ₹ 1,98,000; ₹ 1,96,000 and ₹ 1,95,000 respectively. They have deposited a sum of ₹ 10,000 each in PPF. Determine the taxable income of the firm and its partners.

Answer/Hint:

1. Resident in India.
4. ₹ 6,33,000
5. Taxable Income of firm ₹ 1,00,000

X: 2,60,000 Y: 2,34,000 Z: 1,85,000

Suggested Readings

1. Girish Ahuja & Ravi Gupta : Professional Approach to Direct Taxes-Law and Practice
2. Dr. V K Singhania : Direct Taxes Law and Practices
3. B.B. Lal and N. Vashist : Direct Taxes, Income Tax, Wealth Tax and Tax Planning

TAXATION OF INDIVIDUALS, PARTNERSHIP FIRMS/LLP AND COMPANIES

PART III: TAXATION OF COMPANIES

After completing this part, a student will be able to:

- Understand the Constitutional Provisions relating to taxation for Companies, Division of Corporate and Income taxes.
- Understand the provisions relating to companies; Minimum Alternate Tax, certain deductions allowed to Company Assessee only, Dividend Distribution Tax etc.

CONSTITUTIONAL PROVISIONS

Under the Constitution, Entry 85 of the Union List in the Seventh Schedule specifies Corporation tax as a tax on companies.

Article 366(6) defines corporate tax as follows:

Corporate tax means any tax on income, so far as that tax is payable by companies and is a tax in case the following conditions are fulfilled:

- (i) It is not chargeable in respect of agricultural income;
- (ii) No deduction in respect of tax paid by companies is by any enactments which may apply to the tax authorised to be made from dividends payable by the companies to individuals;
- (iii) No provision exists for taking the tax so paid into account for computation for the purposes of Indian income tax, the total income of individuals receiving such dividends, or in computing the Indian income tax payable by, or refundable to, such individuals.

MEANING OF COMPANY

As per Section 2(17) of the Income-tax Act, 1961 ('the Act'), company means:

- (i) Any Indian Company; or
- (ii) Any body corporate incorporated by or under the laws of a country outside India; or
- (iii) Any institution, association or body which is or was assessable or was assessed as a company for any assessment year under the Income-tax Act, 1922 or was assessed under this Act, as a company for any assessment year commencing on or before April 1, 1970; or
- (iv) Any institution, association or body, whether incorporated or not and whether Indian or non-indian, which is declared by general or special order of the CBDT to be a company.

Provided that such institution, association or body shall be deemed to be a company only for such assessment year or assessment years (whether commencing before the 1st day of April, 1971 or thereafter) as may be specified in the declaration.

Note 1: A statutory corporation established under the Act of Parliament, Government Companies and the State Government companies who carry on a trade or business would also be treated as a company for all purposes of Income tax.

CATEGORIES OF COMPANIES

For the purposes of Income tax, companies can be divided into following categories:



INDIAN COMPANY

As per Section 2(26) of the Act, Indian Company means a company formed and registered under the Companies Act, 1956 and includes:

- (a) A company formed and registered under any law relating to companies formerly in force in any part of India (other than the State of Jammu & Kashmir, and the Union Territories specified in (e) below);
- (b) Any corporation established by or under a Central, State or Provincial Act;
- (c) Any institution, association or body declared by the Board to be a company under section 2(17) of the Act;
- (d) In the case of Jammu & Kashmir, any company formed and registered under any law for the time being in force in that State; and
- (e) In the case of any of the Union Territories of Dadra and Nagar Haveli, Daman and Diu and Pondicherry, a company formed and registered under any law for the time being in force in that Union Territory;

Provided that the registered or as the case may be, principal office of the company, corporation, institution, association or body in all cases is in India.

The definition of an Indian company has been specifically provided under the Income tax act because of the fact that Indian companies are entitled to certain special tax benefits under the Act.

DOMESTIC COMPANY

Section 2(22A) defines domestic company as an Indian company or any other company which, in respect of its income liable to tax under the Income-tax Act, has made the prescribed arrangements for the declaration and payment within India, of the dividends (including dividends on preference shares) payable out of such income.

Thus, all Indian companies are domestic companies. However, a non-Indian company would be a domestic company only if it makes the following prescribed arrangements for the declaration and payment of dividends in India:

- (a) The share register of the company concerned, for all its shareholders, shall be regularly maintained at its principal place of business within India in respect of any assessment year from a date not later than the first day of April of such year;
- (b) The general meeting for passing the accounts of the previous year relevant to the assessment year declaring any dividends in respect thereof shall be held only at a place within India;
- (c) The dividends declared, if any, shall be payable only within India to all shareholders.

FOREIGN COMPANY

Section 2(23A) defines foreign company as a company which is not a domestic company. However, all non-Indian companies are not foreign companies as a non-indian company can be a domestic company if it makes the above-mentioned prescribed arrangements for the declaration and payment of dividends in India.

COMPANY IN WHICH PUBLIC ARE SUBSTANTIALLY INTERESTED (A WIDELY HELD COMPANY)

As per Section 2(18), a company is said to be one in which public are substantially interested in the following cases, namely:

- (i) If it is a company owned by the Government or RBI or in which at least 40% of the shares, whether singly or taken together, are held by the Government or RBI or a corporation owned by RBI; or
- (ii) If it is a company registered under Section 25 of the Companies Act, 1956; or
- (iii) If it is a company, having no share capital and if, having regard to its objects, the nature and composition of its membership and other relevant considerations, it is declared by an order of the Central Board of Direct Taxes (CBDT) to be a company in which the public are substantially interested;
- (iv) If it is a company which carries on its as its principal business, the business of acceptance of deposits from its members and which is declared by the Central Government under Section 620A of the Companies act, 1956 to be a Nidhi or Mutual Benefit Society; or
- (v) If it is company in which shares carrying atleast 50% of the voting power have been allotted unconditionally to or acquired unconditionally by, and are throughout the relevant previous year beneficially held by, one or more cooperative societies; or
- (vi) If it is company which is not a private company as defined in Section 3 of the Companies Act, 1956 and equity shares of the company were, as on the last day of the relevant previous year, listed in a recognised stock exchange in India;
- (vii) If it is a company which is not a private company and the shares in the company (other than preference shares) carrying atleast 50% (40% in case of an Industrial company) of the voting power have been allotted unconditionally to, or acquired unconditionally by, and were throughout the relevant accounting year beneficially held by (a) Government, or (b) a corporation establishment by a Central or State or Provincial Act, or (c) any company in which the public are substantially interested or a wholly owned subsidiary company.

Note: Industrial company means an Indian company where business consists mainly in the construction of ships or in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power.

CLOSELY HELD COMPANY

A Company in which the Public is not substantially interested is known as a closely held company.

The distinction between a closely held and widely held company is significant from the following viewpoints:

- (i) Section 2(22)(e) which deems certain payments as dividend is applicable only to the shareholders of a closely held company; and
- (ii) A closely held company is allowed to carry forward its business losses only if the conditions specified in section 79 are satisfied.

TAX INCIDENCE ON COMPANY

Incidence of tax depends upon the residential status of a person. A company may be resident or non-resident in India.

As per Section 6(3), a company is resident in India in any previous year, if

- (i) It is an Indian company; or
- (ii) During that year, the control and management of its affairs is situated wholly in India;

Therefore, if any of the above two tests is not satisfied, the company would be a non-resident in India during that previous year.

According to Section 5(1) of the Act, the total income of a resident company would consist of:

- (i) Income received or deemed to be received in India during the previous year by or on behalf of such company;
- (ii) Income which accrues or arises or is deemed to accrue or arises to it in India during the previous year;
- (iii) Income which accrues or arises to it outside India during the previous year;

Under Section 5(2) of the Act, the total income of a non-resident company would consist of:

- (i) Income received or deemed to be received in India during the previous year by or on behalf of such company;
- (ii) Income which accrues or arises or is deemed to accrue or arises to it in India during the previous year;

RATES OF INCOME TAX FOR THE ASSESSMENT YEAR 2014-15

(i) Domestic Companies

For income other than long term capital gains : 30% of total income

On short term capital gains emanating from transfer of a short term capital asset being an equity share or unit of an equity oriented fund : 15% of such short term capital gains

On long term capital gains emanating from transfer of a long term capital asset : 20%

Note: 1. Surcharge @ 5% is applicable if total income of the domestic company exceeds ₹ one crore but does not exceed ₹ ten crores. Surcharge @ 10% shall be levied if total income of domestic company exceeds ₹ ten crores.

2. Education cess @ 2% and Secondary & Higher education cess (SHEC) @ 1% is levied on tax including surcharge.

(ii) Foreign Companies

In the case of a company other than a domestic company

On so much of the total income as consists of royalties received from Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern after the 31st March 1961 but before 1st April, 1976; or fees for technical services received from Government or an Indian concern in pursuance of an agreement made by it with the Government or the Indian concern after 29th February, 1964

but before 1st April, 1976, and such agreement has, in either case, been approved by the Central Government : **50% of such royalty or fees for technical services, as the case may be;**

On other incomes: 40% of such income

Note: 1. Surcharge @ 2% is applicable if total income of the domestic company exceeds ₹ one crore but does not exceed ₹ ten crores. Surcharge @ 5% shall be levied if total income of domestic company exceeds ₹ ten crores.

2. Education cess @ 2% and Secondary & Higher education cess (SHEC) @ 1% is levied on tax including surcharge.

Marginal Relief: However, in case of domestic as well as other companies, the total amount payable as income-tax and surcharge on total income exceeding one crore rupees but not exceeding ten crore rupees, shall not exceed the total amount payable as income-tax on a total income of one crore rupees, by more than the amount of income that exceeds one crore rupees.

The total amount payable as income-tax and surcharge on total income exceeding ten crore rupees, shall not exceed the total amount payable as income-tax and surcharge on a total income of ten crore rupees, by more than the amount of income that exceeds ten crore rupees.

Marginal relief is not available in respect of Education cess and SHEC.

MINIMUM ALTERNATE TAX (MAT)

Rationale behind introducing MAT provisions is provided in the Explanatory Memorandum to the Finance Bill, 2000 which was to levy tax on companies paying zero/nominal taxes while having considerable amount of book profits.

MAT provisions are provided in Section 115JB of the Act. As per Section 115JB, all companies having book profits under the Companies Act shall have to pay MAT at the rate of 18.5%. According to section 115JB, if the income tax payable by a company on its total income as computed under the Act in respect of any previous year relevant to the Assessment year commencing on or after 1st April, 2012 is less than 18.5% of such book profit then the tax payable for the relevant previous year shall be deemed to be 18.5% of such book profit. Surcharge and cess shall be levied separately on such amount.

As per Section 115JB(2), A company will prepare its profit and loss account for the relevant previous year in accordance with the provisions of Part II of Schedule VI of the Companies Act, 1956. However, while preparing the annual accounts including profit and loss account:

- (a) The accounting policies;
- (b) The accounting standards followed for preparing such accounts including profit and loss accounts; and
- (c) The methods and rates adopted for calculating the depreciation,

shall be the same as have been adopted for the purpose of preparing such accounts including profit and loss account and laid before the company at its annual general meeting in accordance with the provisions of Section 210 of the Companies Act, 1956.

However, where the company has adopted or adopts the financial year different from previous year, (a), (b) and (c) aforesaid shall correspond to the accounting policies, accounting standards and the method and rates for calculating the depreciation which have been adopted for preparing such accounts including profit and loss account for such financial year or part of such financial year falling within the relevant previous year.

As per section 115JB, every company is required to prepare its accounts as per Schedule VI of the Companies Act, 1956. However, as per the provisions of the Companies Act, 1956, certain companies, e.g. Insurance, Banking or Electricity Company, are allowed to prepare their profit and loss account in accordance with the provisions specified in their regulatory Acts.

In order to align the provisions of Income-tax Act with the Companies Act, 1956, with effect from assessment year 2013-14, section 115JB has been amended to provide that the companies which are not required under section 211 of the Companies Act to prepare their profit and loss account in accordance with the Schedule VI of the Companies Act, 1956, profit and loss account prepared in accordance with the provisions of their regulatory Acts shall be taken as a basis for computing the book profit under section 115JB.

Meaning of Book Profit

As per explanation below Section 115JB(2), Book Profit means the net profit as shown in the profit and loss account for the relevant previous year prepared under Section 115JB(2) as increased by the following amounts:

- (a) The amount of income tax paid or payable and the provision thereof; or
- (b) The amounts carried to any reserve other than shipping reserve u/s 33AC of the Act; or
- (c) The amount or amounts set aside to provisions made for meeting unascertained liabilities; or
- (d) The amount by way of provision for losses of subsidiary companies; or
- (e) The amount or amounts of dividends paid or proposed; or
- (f) The amount or amounts of expenditure relatable to any income to which section 10 [other than section 10(23G) or 10(38)] or section 11 or section 12 apply;
- (g) The amount of depreciation; or
- (h) The amount of deferred tax and provisions thereof; or
- (i) The amount or amounts set aside as provision for diminution in the value of any asset.
- (j) The amount standing in revaluation reserve relating to revalued asset on the retirement or disposal of such asset.

The net profit as increased by the amounts referred to in Clauses (a) to (j) shall be reduced by the following amounts:

- (i) The amount withdrawn from any reserves or provisions if any such amount is credited to the profit and loss account;
Provided that the amount withdrawn from reserves created or provisions made in a previous year shall not be reduced from the book profit unless the book profit of such year or any earlier year has been increased by those reserves or provisions (out of which the said amount was withdrawn);
- (ii) The amount of income to which any of the provisions of Section 10 or Section 11 or Section 12 apply, if any such amount is credited to the profit and loss account; or
- (iia) the amount of depreciation debited to the profit and loss account (excluding the depreciation on account of revaluation of assets); or
- (iib) the amount withdrawn from revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to

- in Clause (iia); or
- (iii) The amount of loss brought forward or unabsorbed depreciation, whichever is less, as per books of account.
- For the purposes of this clause, the loss shall not include depreciation. Therefore, in a case where an assessee has shown profit in a year, but after adjustment of depreciation it results in a loss, no adjustment in book profit is allowed; or
- (iv) The amount of profits of sick industrial company for the assessment year commencing on and from the assessment year relevant to the previous year in which the said company has become a sick industrial company under Section 17(1) of the Sick Industrial Companies (Special Provisions) Act, 1985 ('SICA') and ending with the Assessment year during which the net worth (as per section 3 of the SICA) of such company becomes equal to or exceeds the accumulated losses.
- (v) The amount of deferred tax, if any such amount is credited to the profit and loss account.

Notes:

- (1) Nothing contained in Section 115JB shall affect the determination of the amounts of unabsorbed depreciation under Section 32(2), business loss under Section 72(1), speculation loss u/s 73, Capital loss u/s 74 and loss u/s 74A in relation to the relevant previous year to be carried forward to the subsequent year or years.
- (2) Every company to which this section applies, shall furnish a report in the prescribed form from an accountant as defined in the Explanation below Section 288(2) certifying that the book profit has been computed in accordance with the provisions of Section 115JB, alongwith the return of income.
- (3) Save as otherwise provided in Section 115JB, all other provisions of the Act shall apply to every assessee, being a company, mentioned in this section.
- (4) The provisions of Section 115JB shall apply to the income accrued or arising on or after 1st April, 2005 from any business carried on, or services rendered, by an entrepreneur or a Developer, in a Unit or SEZ (Special Economic Zone), as the case may be (amendments made by Finance Act, 2011 and shall be effective from AY 2012-13, earlier the MAT provisions did not apply to SEZ enterprises and SEZ developers).
- (5) Provisions of MAT on the book profits of a Company would not apply to a Foreign Company not having any physical presence in India [AAR in case of Timken India Ltd. (2003) 273 ITR 67]. In order to comply with the requirement of MAT provisions regarding Profit and Loss Account in accordance with the provisions of the Indian Companies Act, it is essential that the foreign company should have a place of business in India.

MAT CREDIT

MAT credit is available as per Section 115JA. Credit of MAT in respect of excess of tax paid under Section 115JB (i.e. difference of tax on normal income and tax on Book profit) to the extent that after such credit, tax payable should not be less than 18.5% of book profits for the relevant previous year, will be available and it can be carried forward to 10 Assessment years.

Illustration

The book profits of a company in the previous year 2013-14 computed in accordance with section 115JB is ₹ 15 lakh. If the total income computed for the same period as per the provisions of the Income-tax Act, 1961 is ₹ 3 lakh, calculate the tax payable by the company in the assessment year 2014-15 and also indicate whether the company is eligible for any tax credit.

Solution**Calculation of tax payable by the Company for AY 2014-15 (Previous Year 2013-14):**

Particulars	Amount (₹)
Tax on total income @ 30.9% (including cess) $[3,00,000 \times 30.9\%]$	92,700
Tax on Book profits @ 19.055% (including cess) $[15,00,000 \times 19.055\%]$	2,85,825

The company will have to pay tax of ₹ 2,85,825 as tax on the basis of book profits exceeds the tax payable as per the normal provisions of the Act.

However, company will be eligible for tax credit of the difference of tax on book profits and tax on total income as per normal provisions of the Act. In this case, tax credit amounts to ₹ 1,93,125 which can be adjusted in subsequent 10 Assessment years in that year/s in which tax payable as per normal provisions exceeds that payable under the provisions of section 115JB.

Illustration

DEF Ltd.'s details of Income for Financial Year 2013-14 is as follows:

	₹
Sale proceeds (domestic)	32,00,000
Export proceeds	6,30,000
Withdrawal from General Reserve	1,50,000
(Reserve was created earlier by debiting Profit & Loss A/c)	
Withdrawn from Revaluation Reserve	80,000
Total	40,60,000
Less: Depreciation (including Dep. on Revaluation of ₹ 70,000)	5,40,000
Salaries	3,60,000
Wealth tax	45,000
Income tax	32,000
Outstanding Custom duty	12,400
Outstanding Excise duty	11,800
Professional fees	50,000
Other business expenses	25,000
Net Profit	29,83,800
Less: Dividend (Proposed)	30,600
Net Profit as per P&L A/c	29,53,200

The company is eligible for following:

- Deduction u/s 80 IB ₹ 4,50,000
- Depreciation u/s 32 ₹ 6,40,000

The company wants to set off the following:

Brought forward loss of F.Y. 2007-08:

- As per Account ₹ 4,00,500
- As per Income Tax Act, 1961 ₹ 10,80,000

Unabsorbed depreciation as per

- Account ₹ 90,000
- Income Tax Act, 1961 Nil

Compute the Total Income and Tax Liability of DEF Ltd. for the A.Y. 2014-15.

Solution:**Computation of Total Income of DEF Ltd. for A.Y. 2014-15**

	₹
Net Profit as per P&L A/c	29,53,200
Add: Depreciation as per P&L A/c	5,40,000

Less: Depreciation as per Income Tax Act	(6,40,000)
Add: Outstanding Custom and Excise Duty (assumed not paid upto due date of return)	24,200
Add: Income tax	32,000
Add: Wealth tax	45,000
Less: Withdrawal from General Reserve	(1,50,000)
Less: Withdrawal from Revaluation Reserve	(80,000)
Add: Proposed Dividend	30,600
Business Income	27,55,000
<i>Less:</i>	
Brought Forward Losses	(10,80,000)
Business Income/GTI (Presently)	16,75,000
Deduction u/s 80IB	(4,50,000)
Total Income	12,25,000
Tax Liability on Tax Income (under normal provisions) [12,25,000 @ 30%]	3,67,500
Add: Education Cess & SHEC @ 3%	11,025
Tax (normal provisions) (A)	3,78,525

Minimum Alternate Tax (MAT) u/s 115JB

₹

Book Profits:	
Net profit as per P&L A/c	29,53,200
Add: Depreciation as per P&L A/c	5,40,000
– Income tax	32,000
– Proposed Dividend	30,600
Less: Depreciation (other than on revaluation)	(4,70,000)
– Amount withdrawn from General Reserve	(1,50,000)
– Withdrawn from Revaluation Reserve to the extent it does not exceed extra depreciation on Revaluation	(70,000)
Book Profits	28,65,800
Tax Liability @19.055% of Rs. 28,65,800 (B)	5,46,078
Tax Payable u/s 115JB [Higher of A and B]	₹ 5,46,078
MAT Credit u/s 115JB [5,46,078 – 3,78,525]	₹ 1,67,553

DIVIDEND DISTRIBUTION TAX (DDT) (SECTION 115-O)

A domestic company is liable to pay tax on the amounts distributed, declared or paid as dividend (whether interim or otherwise) and it shall be payable @ 15% plus surcharge @ 10% and education cess and SHEC @ 3% in addition to the income tax payable (effective rate therefore would be 16.995%).

Exclusions from DDT

The amount distributed, declared or paid as dividend may be out of accumulated or current year profits and same shall exclude:

- (i) The amount of dividend if any received by the domestic company during the financial year, if such dividend is received from its subsidiary and;
 - (a) Where such subsidiary is a domestic company, the subsidiary has paid tax which is payable under this section on such dividend; or
 - (b) Where such subsidiary is a foreign company, the tax is payable by the domestic company under Section 115BBD on such dividend.

However, the same amount of dividend shall not be taken into account more than once.

Note: A company shall be a subsidiary of another company, if such other company holds more than half in nominal value of the equity share capital of the company.

(ii) The amount of dividend paid to any person for, or on behalf of, the New Pension System Trust referred to in clause (44) of Section 10.

Note: Dividend shall not include deemed dividend u/s 2(22)(e) i.e. loan or advance given by a closely held company to a shareholder holding beneficial interest of 10% or more in the company or loan or advance given by a closely held company to a concern in which the aforesaid shareholder has substantial interest, but include dividend u/s 2(22)(a), (b), (c) or (d).

Applicability of DDT on SEZ

Finance Act, 2011 inserted a proviso to sub-section 6 of Section 115O by which the provisions of Section 115O shall also be applicable on an enterprise or undertaking engaged in developing, operating and maintaining a SEZ.

Time limit for payment

The amount of such tax shall be deposited within 14 days from earliest of the following dates:

- (a) Declaration of dividend; or
- (b) Distribution of dividend; or
- (c) Payment of dividend

Deduction of DDT not allowable

Any amount paid as DDT shall not be allowed as deduction under the provisions of the Act.

Amendment by Finance Act, 2013

Section 115-O is amended in order to remove the cascading effect in respect of dividends received by a domestic company from a similarly placed foreign subsidiary (i.e. the foreign company in which domestic company holds more than fifty per cent of equity share capital). It is proposed that where the tax on dividends received from the foreign subsidiary is payable under section 115BBD by the holding domestic company then, any dividend distributed by the holding company in the same year, to the extent of such dividends, shall not be subject to Dividend Distribution Tax under section 115-O of the Income-tax Act.

This amendment will take effect from 1st June, 2013.

Illustration

Compute the liability towards dividend distribution tax under section 115-O in following cases:

1. *A domestic company engaged in the business of growing and manufacturing tea in India, has declared a final dividend of ₹ 10 lakh for the financial year 2013-14.*

Solution

In this case, tax would only be levied only on the amount of non-agricultural income i.e. 40% of ₹ 10 lakhs (₹4 lakhs). Tax would be levied under section 115-O at effective rate of 16.995%, which amounts to ₹ 67,980.

As per the decision of Calcutta High Court in case of Jayshree Tea and Industries Ltd. v. UOI [2006] 285 ITR 506, the tax on distributed profits is a tax on the company and not on shareholders. Therefore, the distributed profits retain the same character as that of the income being distributed.

Therefore, in case of a company engaged in agricultural activities in India, tax on distributed profits shall be levied only on the amount of non-agricultural income i.e. 40% of the amount declared as dividend of ₹ 10 lakhs. Therefore, tax liability of company would be ₹ 67,980 as calculated above.

2. *A foreign company which has made prescribed arrangements for declaration and payment of dividends within India, pays preference share dividend of ₹ 100 lakh for financial year 2013-14.*

Solution

A foreign company, which has made prescribed arrangements for declaration and payment of dividends within India, will be a domestic company [Section 2(22A)].

Therefore, in the above case, the foreign company is a domestic company and it would be liable to pay a dividend distribution tax of 16.995% on ₹ 100 lakhs which amounts to ₹ 16,99,500.

TAXATION OF FOREIGN DIVIDENDS (SECTION 115BBD)

As per Section 115BBD(1), Where the total income of an assessee, being an Indian company, for the previous year relevant to the assessment year beginning includes any income by way of dividends declared, distributed or paid by a specified foreign company, the income-tax payable shall be the aggregate of—

- (a) the amount of income-tax calculated on the income by way of such dividends, at the rate of fifteen per cent; and
- (b) the amount of income-tax with which the assessee would have been chargeable had its total income been reduced by the aforesaid income by way of dividends.

The aforesaid amount would be increased by the applicable surcharge and cess.

Deduction in respect of any expenditure or allowance shall not be allowed to the assessee under any provision of this Act in computing its income by way of aforesaid dividends

Notes:

- (i) "dividends" shall have the same meaning as is given to "dividend" in clause (22) of section 2 but shall not include sub-clause (e) thereof;
- (ii) "specified foreign company" means a foreign company in which the Indian company holds twenty-six per cent or more in nominal value of the equity share capital of the company.

In order to continue the tax incentive for one more year, section 115BBD is amended to extend the applicability of this section in respect of income by way of dividends received from a specified foreign company in Financial Year 2013-14 also, subject to the same conditions.

SELF TEST QUESTIONS

(These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.)

1. Define the following keeping in view the points involved while planning tax:
 - (a) Indian company
 - (b) Domestic company
 - (c) Foreign company
 - (d) Company in which public is substantially interested
 - (e) Closely held company

2. Explain the significance of classification of companies under the Income tax Act, 1961 and their impact on the tax liability.
 3. Explain how is the residential status of a company determined under the Income-tax Act, 1961.
 4. Explain how (i) the scope of tax liability on total income and (ii) rate of tax applicable to a company, are determined?
 5. Explain the concept of MAT and its rationale.
 6. TA Ltd. is a company registered in India. All its decisions are taken from India. Determine its residential status for AY 2014-15.

Answer/Hint: Resident in India.

7. TA Ltd. is a company incorporated outside India but all its board meetings are held in India during PY 2013-14. Determine its residential status for AY 2014-15.

Answer/Hint: Resident in India.

8. Write short notes on the following:

- (i) Dividend Distribution Tax
 - (ii) MAT Credit

9. What do you understand by "Book Profit" in the context of Minimum Alternate tax.

Suggested Readings

1. Girish Ahuja & Ravi Gupta : Professional Approach to Direct Taxes-Law and Practice
 2. Dr. V K Singhania : Direct Taxes Law and Practices
 3. B.B. Lal and N. Vashist : Direct Taxes, Income Tax, Wealth Tax and Tax Planning

Lesson 2

International Taxation

LESSON OUTLINE

THIS LESSON IS DIVIDED INTO FOUR PARTS

- I. TAXATION OF NON-RESIDENT ENTITIES
- II. ADVANCE RULING
- III. TRANSFER PRICING
- IV. DOUBLE TAXATION AVOIDANCE AGREEMENTS

LEARNING OBJECTIVES

After the liberalization of Indian economy and easing of restrictions on the entry of foreign entities, cross border business transactions have increased manifold. With the ratification of WTO by the Government of India, our economy has become robust and an atmosphere has sprung up where FII investments in India have increased tremendously. All these economic activities has ramifications for tax laws of the country. Issues like tax havens, transfer pricing, double taxation, WTO, Subpart F, etc. are required to be taken care of and have become part and parcel of international taxation regime.

After completion of this lesson the students will understand

- The basic principle for taxation of International Transaction
- Provisions for taxation of non-residents
- How a person can avail the benefit of double taxation treaties
- Transfer pricing provisions such as documentation, computation of Arm's Length price etc.
- The impact of transfer pricing
- In what circumstances a person can seek advance ruling.

International taxation covers the taxation of persons or business subject to tax law of different countries. In broader sense the concept of International Taxation includes domestic legislation covering foreign income of resident (globally) and domestic income of non-residents.

INTERNATION TAXATION

PART I: TAXATION OF NON-RESIDENTS

Under the Income-Tax Act, worldwide Income of a Resident person is taxable in India. However in respect of a Non-Resident, only that Income which is received or deemed to have been received in India by or on his behalf and income that accrues or arises or is deemed to accrue or arising in India is taxable in India. Let's discuss the provisions contained under the Income Tax Act for taxability of Non-resident.

After completion of this Part, student will:

- have the understanding of taxation provisions for Non-Residents.
- be aware of circumstances under which Non-Residents income is taxable.
- be familiar with exemptions available with the Non-Residents.
- have the understanding of special provisions for computation of Income of Non-Residents.

WHO IS A NON-RESIDENT?

NON RESIDENT INDIVIDUAL

As per section 6, Individual will be non resident if he does not satisfy any of the two basic conditions:

- (i) Stay in India for 182 days or more during relevant previous year; or
- (ii) Stay in India for 62 days or more during relevant previous year and 365 days or more during 4 previous years immediately preceding relevant previous year.

However, in following cases, the 2nd basic condition will not be checked. If individual satisfies 1st basic condition, then he will be resident, otherwise non-resident.

- (a) Indian Citizen:
 - going abroad for employment purposes during relevant previous year.
 - being a crew member of an Indian Ship
 - coming on a visit to India during relevant previous year.
- (b) Person of Indian Origin (Person who himself, his parents or his grandparents were born in undivided India)
 - coming on a visit to India during relevant PY

NON-RESIDENT HINDU UNDIVIDED FAMILY (HUF)

HUF will be non-resident if its control & management of its business affairs is wholly situated outside India.

Control & management is said to be situated at that place where major decisions relating to business are taken.

NON RESIDENT COMPANY

Only a foreign company (company which is not registered in India) can be non resident when control & management of its business affairs is wholly or partly situated outside India.

NON RESIDENT FIRM OR LLP/AOP OR BOI/LOCAL AUTHORITY/ARTIFICIAL JURIDICAL PERSON

These persons would be non resident in India when control & management of their business affairs is wholly situated outside India.

TAX INCIDENCE ON NON RESIDENT (SECTION 5)

Total income of any previous year of a person who is a non-resident includes all income from whatever source derived which;

- is received in India
- is deemed to be received in India
- is accrued or arisen in India
- is deemed to accrue or arise in India

Income deemed to accrue or arise in India (Section 9)

As per section 9, the following incomes shall be deemed to accrue or arise in India;

Business Connection

All income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.

“Business connection” shall include any business activity carried out through a person who, acting on behalf of the non-resident,—

- (a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident; or
- (b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or
- (c) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident:

However, such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business.

Further, an agent working mainly for Non-Resident or, that Non-Resident and other Non-Residents who exercise control over one another or are under common control is not regarded as having an independent status.

Income not to be treated as arising from or through Business Connection

- (a) Income reasonably attributable to the operations carried out in India will be deemed to accrue or arise in India in case all the operations of a business are not carried out in India;

If the income from Indian operations cannot be definitely ascertained, then, the same may be

computed by apportionment:

- at such percentage of Indian turnover as determined by the Assessing Officer;
 - Taxable profits = Total profits × Receipts accruing/arising in India/Total receipts of business; or
 - in any other manner as considered suitable by Assessing Officer
- (b) Income of a Non-Resident in respect of operations confined to purchase of goods in India for the purpose of export;
- (c) Non-Resident engaged in business of running a news agency/publishing newspapers, magazines, journals, income arising through and from activities confined to collection of news and views in India for transmission out of India shall not be deemed to accrue or arise in India.
- (d) Income arising through or from operations confined to shooting of any cinematograph films in India to a Non-Resident being:
- An Individual who is not an Indian citizen
 - A firm not having a partner who is either an Indian citizen or Resident in India; and
 - A company not having any shareholder who is either Indian citizen or Resident in India.

Salaries earned in India

Income from Salaries is treated as earned in India if it is payable for services rendered in India or it is paid for the rest period or leave period preceded and succeeded by services rendered in India and forms part of the service contract of employment

Salaries payable by Government of India to Indian Citizen abroad

Incomes chargeable under the head "Salaries" payable by the GOI to an Indian citizen for services rendered outside India. However, allowances and perquisites received by such Indian citizen are exempt u/s 10.

Dividend by Indian Company

Dividend paid by an Indian company outside India.

Interest Income

Interest income payable by:

- Government of India; or
- A Resident except where it is payable in respect of any debt incurred, or moneys borrowed and used.
 - for the purpose of business or profession carried on by such person outside India; or
 - for the purposes of making or earning any income from any source outside India.
- A Non-Resident, where it is payable in respect of any debt incurred, or moneys borrowed and used for:
 - the purposes of a business or profession carried on by such person in India

Royalty Income

Royalty payable by:

- Government of India

- A Resident except where it is payable in respect of any right, property or information used or services utilised
 - for the purpose of business or profession carried on by such person outside India; or
 - for the purposes of making or earning any income from any source outside India;
- A Non-Resident, where it is payable in respect of any right, property or information used or services utilised
 - for the purposes of a business or profession carried on by such person in India; or
 - for the purposes of making or earning any income from any source in India

Meaning of Royalty [Explanation to Section 9(1)(vi)]: Royalty means consideration including lump-sum consideration for:

- (a) Transfer of all or any rights (including granting of a licence) in respect of any patent, invention, model, design, secret formula or process, trademark or similar property;
- (b) Use or right to use any industrial, commercial or scientific equipment but not including the amount referred to in Section 44BB;
- (c) Imparting of any information concerning the working of or the use of a patent, invention, model, design, secret formula or process, trade mark or similar property;
- (d) Imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;
- (e) Use of any patent, invention, model, design, secret formula or process, trademark or similar property;
- (f) Rendering of any services in connection with activities from (a) to (e) above;
- (g) Transfer of all or any rights (including the granting of a licence) in respect of any copyright, literary, artistic or scientific work including films or videotapes for use in connection with radio broadcasting but not including consideration for the sale, distribution or exhibition of cinematographic films.

Exclusions: The following shall not be treated as royalty:

- (a) Any consideration chargeable as income of recipient as Capital gains;

Fees for Technical Services (FTS)

FTS payable by:

- Government of India
- A Resident, except where it is payable in respect of services utilised:
 - in a business or profession carried on by such person outside India; or
 - for the purposes of making or earning any income from any source outside India
- A Non-Resident, where it is payable in respect of any services utilised
 - in a business or profession carried on by such person in India; or
 - for the purposes of making or earning any income from any source in India

Meaning of Fees for Technical Services [Explanation to Section 9(1)(vii)]

Fees for Technical Services means

- any consideration (including any lump sum consideration) for the rendering of any
- managerial, technical or consultancy services (including provision of services of technical or other personnel).

Exclusions:

Consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head Salaries, shall not be treated as FTS.

Explanation for Interest, Royalty and FTS: Interest, Royalty and FTS taxable even if no territorial connection of Non-Resident with India or even if services not actually rendered in India, income of a Non-Resident shall be deemed to accrue or arise in India u/s 9(1)(v)/(vi)/(vii) and shall be included in the total income of the Non-Resident, whether or not-

- (i) the Non-Resident has a residence or place of business or business connection in India; or
- (ii) the Non-Resident has rendered services in India

INCOMES EXEMPT IN THE HANDS OF NON-RESIDENT /FOREIGN COMPANY [SECTION 10]

The following incomes are exempt in the hands of a non-resident or a foreign company:

- (a) **Interest on NRE A/c [Section 10(4)(ii)]:** In the case of an individual, any income by way of interest on moneys standing to his credit in a Non-Resident (External) Account in any bank in India in accordance with the *Foreign Exchange Management Act, 1999* ('FEMA') is exempt.
- Individual is a person resident outside India as defined in Section 2 of the FEMA or is a person who has been permitted by the Reserve Bank of India to maintain the aforesaid Account ;
- (b) **Tax payable on Royalty or FTS on behalf of foreign company:** Tax payable, under the terms of the agreement, on Royalty or FTS on behalf of foreign company is exempt under section 10(6A).

Point to be noted:

- *Such foreign company receives such income from GOI or an Indian concern in pursuance of an agreement made before 1/6/2002.*
- *Agreement must be in accordance with Industrial Policy or approved by the Central Government*

- (c) **Tax payable on certain incomes on behalf of foreign company or NR:** Tax payable on certain incomes (not being salary, royalty or FTS) on behalf of foreign company or a NR is exempt u/s 10(6B).

Point to be noted:

- *Income is earned in pursuance of agreement made before 1/6/2002 between CG and Government of foreign state/international organisation.*
- *Tax is payable as per the agreement by the Government or Indian Concern.*

- (d) **Tax payable by Indian Company on behalf of foreign Govt. etc.:** Tax payable, on behalf of foreign Govt. or foreign enterprises by, Indian company engaged in business of operation of aircraft, on income from leasing of aircraft etc. u/s 10(6BB).

Point to be noted:

- The payment is as consideration for acquiring an aircraft/aircraft engine on lease under an agreement and not for providing spares, facilities or services in connection with the operation of a leased aircraft.
- The agreement is entered after 31/3/2007 and is approved by the Central Government.

(e) Royalty or FTS received by a specified foreign company: Royalty or FTS received by specified foreign company is exempt u/s 10(6C).

Point to be noted:

Income is received under agreement entered into with Central Government for providing services in or outside India in projects related with security of India.

(f) Lease rent paid for leasing aircraft Leasing rent paid for leasing aircraft by an Indian company engaged in business of operation of aircraft as a consideration for acquiring an aircraft or an aircraft engine on lease from Govt. of a foreign State or a foreign enterprise under an agreement is exempt under section 10(15A) in the hands of NR or foreign company..

Point to be noted:

- The payment should not be for providing spares, facilities or services in connection with the operation of leased aircraft.
- No exemption shall be available for agreement entered into on or after 1/4/2007.

SPECIAL PROVISIONS FOR COMPUTING PROFITS AND GAINS IN CASE OF NON-RESIDENTS [DEEMED/PRESUMPTIVE INCOME/TAXATION]

A. SECTION 44B: SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF SHIPPING BUSINESS IN THE CASE OF NON-RESIDENTS

Notwithstanding anything to the contrary contained in section 28 to 43A, in the case of a Non resident engaged in the business of operation of ships, a sum equal to seven and a half per cent of the aggregate of the following amounts shall be deemed to be the profits and gains of such business chargeable to tax under the head PGBP:

- (i) the amount paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods shipped at any port in India; and
- (ii) the amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods shipped at any port outside India.

Note: The aforesaid amounts shall include the amount paid or payable or received or deemed to be received, as the case may be, by way of demurrage charges or handling charges or any other amount of similar nature.

B. SECTION 44BB: SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS IN CONNECTION WITH THE BUSINESS OF EXPLORATION, ETC., OF MINERAL OILS.

Notwithstanding anything to the contrary contained in sections 28 to 41 and sections 43 and 43A, in the case of an assessee being a non-resident, engaged in the business of providing services or facilities in connection with, or supplying plant and machinery on hire used, or to be used, in the prospecting for, or extraction or

production of, mineral oils, a sum equal to ten per cent of the aggregate of the following amounts shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession":

- (a) the amount paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils in India; and
- (b) the amount received or deemed to be received in India by or on behalf of the assessee on account of the provision of services and facilities in connection with, or supply of plant and machinery on hire used, or to be used, in the prospecting for, or extraction or production of, mineral oils outside India.

Point to be noted:

- *Section 44BB will not apply in a case where the provisions of sections 42, 44DA, 115A and 293A apply for computing profits or gains or any other income referred to therein.*
- *An assessee may claim lower profits and gains than the profits and gains specified in that sub-section, if he keeps and maintains such books of account and other documents as required under sub-section (2) of section 44AA and gets his accounts audited and furnishes a report of such audit as required under section 44AB, and thereupon the Assessing Officer shall proceed to make an assessment of the total income or loss of the assessee under sub-section (3) of section 143 and determine the sum payable by, or refundable to, the assessee.*

C. SECTION 44BBA: NR SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF THE BUSINESS OF OPERATION OF AIRCRAFT IN THE CASE OF NON-RESIDENTS.

Notwithstanding anything to the contrary contained in sections 28 to 43A, in the case of an assessee, being a non-resident, engaged in the business of operation of aircraft, a sum equal to five per cent of the aggregate of the following amounts shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession":

- (a) the amount paid or payable (whether in or out of India) to the assessee or to any person on his behalf on account of the carriage of passengers, livestock, mail or goods from any place in India; and
- (b) the amount received or deemed to be received in India by or on behalf of the assessee on account of the carriage of passengers, livestock, mail or goods from any place outside India.]

D. SECTION 44BBB: SPECIAL PROVISION FOR COMPUTING PROFITS AND GAINS OF FOREIGN COMPANIES ENGAGED IN THE BUSINESS OF CIVIL CONSTRUCTION, ETC., IN CERTAIN TURNKEY POWER PROJECTS

Notwithstanding anything to the contrary contained in sections 28 to 44AA, in the case of an assessee, being a foreign company, engaged in the business of civil construction or the business of erection of plant or machinery or testing or commissioning thereof, in connection with a turnkey power project approved by the Central Government in this behalf, a sum equal to ten per cent of the amount paid or payable (whether in or out of India) to the said assessee or to any person on his behalf on account of such civil construction, erection, testing or commissioning shall be deemed to be the profits and gains of such business chargeable to tax under the head "Profits and gains of business or profession".

An assessee may claim lower profits and gains than the profits and gains specified above, if he keeps and maintains such books of account and other documents as required under sub-section (2) of section 44AA

and gets his accounts audited and furnishes a report of such audit as required under section 44AB, and thereupon the Assessing Officer shall proceed to make an assessment of the total income or loss of the assessee under sub-section (3) of section 143 and determine the sum payable by, or refundable to, the assessee.

E. SECTION 172 SHIPPING BUSINESS OF NON-RESIDENTS:

- (a) **Applicability:** The provisions of this section shall apply for the purpose of the levy and recovery of tax in the case of any ship, belonging to or chartered by a non-resident, which carries passengers, livestock, mail or goods shipped at a port in India.
- (b) **Deemed Income:** Where such a ship carries passengers, livestock, mail or goods shipped at a port in India, seven and a half per cent of the amount paid or payable on account of such carriage to the owner or the charterer or to any person on his behalf, whether that amount is paid or payable in or out of India, shall be deemed to be income accruing in India to the owner or charterer on account of such carriage.
- (c) Before the departure from any port in India of any such ship, the master of the ship shall prepare and furnish to the Assessing Officer a return of the full amount paid or payable to the owner or charterer or any person on his behalf, on account of the carriage of all passengers, livestock, mail or goods shipped at that port since the last arrival of the ship thereat.

However, where the Assessing Officer is satisfied that it is not possible for the master of the ship to furnish the return before the departure of the ship from the port and provided the master of the ship has made satisfactory arrangements for the filing of the return and payment of the tax by any other person on his behalf, the Assessing Officer may, if the return is filed within thirty days of the departure of the ship, deem the filing of the return by the person so authorised by the master as sufficient compliance with the provision.

- (d) **Assessment of Income:** On receipt of the return, the Assessing Officer shall assess the shipping income and determine the sum payable as tax thereon @ 40% (plus applicable surcharge and cess) and such sum shall be payable by the master of the ship.

Order assessing the income and determining the sum of tax payable thereon shall be made within nine months from the end of the financial year in which the return under sub-section (3) is furnished.

- (e) **Claim for Assessment under normal provisions:** Before expiry of AY relevant to PY in which the ship departed, the owner/charterer may claim that assessment of his total income and tax payable be made as per the other provisions of the Act. In that case, any tax paid u/s 172 shall be treated as payment of advance tax leviable for that AY and the difference between the sum so paid and the amount of tax found payable by him, shall be paid by him, or refunded to him.

F. SECTION 44C: DEDUCTION OF HEAD OFFICE EXPENDITURE IN THE CASE OF NON-RESIDENTS.

In the case of a non-resident, expenditure in the nature of head office expenditure will only be allowed as deduction while computing business income to the extent of lower of the following:

- (a) an amount equal to five per cent of the adjusted total income; or
- (b) the amount of head office expenditure incurred by the assessee as is attributable to the business or profession of the assessee in India.

However where the adjusted total income of the assessee is a loss, the amount under clause (a) shall be computed at the rate of five per cent of the average adjusted total income of the assessee.

Notes:

1. Head office expenditure means executive and general administration expenditure incurred by the assessee outside India, including expenditure incurred in respect of—

- (a) rent, rates, taxes, repairs or insurance of any premises outside India used for the purposes of the business or profession;
- (b) salary, wages, annuity, pension, fees, bonus, commission, gratuity, perquisites or profits in lieu of or in addition to salary, whether paid or allowed to any employee or other person employed in, or managing the affairs of, any office outside India;
- (c) travelling by any employee or other person employed in, or managing the affairs of, any office outside India; and
- (d) such other matters connected with executive and general administration as may be prescribed.

2. **Adjusted Total Income** It means total income computed under the Act before deducting following:

- (a) HO expenditure u/s 44C;
- (b) Unabsorbed depreciation u/s 32(2)
- (c) Unabsorbed Capital expenditure on family planning u/s 36
- (d) Carried forward business losses u/s 72
- (e) Speculation losses u/s 73
- (f) Capital losses u/s 74
- (g) Losses from activity of owning and maintaining race horses u/s 74A
- (h) Deduction u/s Chapter VIA

3. **Average Adjusted Total Income** It means the average of adjusted total income of 3 preceding Assessment Years.

However, if the total income of 2 out of 3 preceding Assessment Years or 1 out of 3 preceding Assessment Years was assessable, the average will be computed on the basis of adjusted total income of such 2 or 1 year.

G. SECTION 44DA : SPECIAL PROVISION FOR COMPUTING INCOME BY WAY OF ROYALTIES, ETC., IN CASE OF NON-RESIDENTS

The income by way of royalty or fees for technical services received from Government or an Indian concern in pursuance of an agreement made by a non-resident (not being a company) or a foreign company with Government or the Indian concern after the 31st day of March, 2003, where such non-resident (not being a company) or a foreign company carries on business in India through a permanent establishment situated therein, or performs professional services from a fixed place of profession situated therein, and the right, property or contract in respect of which the royalties or fees for technical services are paid is effectively connected with such permanent establishment or fixed place of profession, as the case may be, shall be computed under the head "Profits and gains of business or profession" in accordance with the provisions of this Act.

However, deduction in respect of following shall not be allowed,—

- (i) in respect of any expenditure or allowance which is not wholly and exclusively incurred for the business of such permanent establishment or fixed place of profession in India; or
- (ii) in respect of amounts, if any, paid (otherwise than towards reimbursement of actual expenses) by the permanent establishment to its head office or to any of its other offices :

Note:

1. Provisions of section 44BB shall not apply in respect of the income referred to in this section.
2. Every non-resident (not being a company) or a foreign company shall keep and maintain books of account and other documents as per section 44AA and get his accounts audited by an accountant and furnish along with the return of income, the report of such audit in the prescribed form duly signed and verified by such accountant.

CHARGE OF TAX ON INCOMES ARISING TO NON-RESIDENTS OR FOREIGN COMPANIES – SPECIAL RATES [SECTION 115A TO 115BBA]

COMPUTATION OF CAPITAL GAINS IN CASE OF TRANSFER BY A NR OF SHARES OR DEBENTURES OF AN INDIAN COMPANY ORIGINALLY PURCHASED IN FOREIGN CURRENCY [1ST PROVISO TO SECTION 48 AND RULE 115A]

In the case of a non-resident, capital gains arising from the transfer of shares in, or debentures of, an Indian company shall be computed by converting the cost of acquisition, expenditure incurred wholly and exclusively in connection with such transfer and the full value of the consideration received or accruing as a result of the transfer of the capital asset into the same foreign currency as was initially utilised in the purchase of the shares or debentures, and the capital gains so computed in such foreign currency shall be reconverted into Indian currency.

The aforesaid manner of computation of capital gains shall also be applicable in respect of capital gains accruing or arising from every reinvestment thereafter in, and sale of, shares in, or debentures of, an Indian company. **[First proviso to Section 48]**

Conversion into foreign currency of purchase [Rule 115A]: Convert Sale consideration, Cost of Acquisition, Expenses on Transfer into foreign currency of purchase on the following rates:

- (a) Sale Consideration: Average exchange rate (Average of Telegraphic Transfer (TT) Buying and Selling rate as per SBI) as on date of transfer.
- (b) Expenses on transfer: Average exchange rate as on date of transfer.
- (c) Cost of Acquisition: Average exchange rate as on date of acquisition

Compute Capital Gains in foreign currency only: Compute capital gains in foreign currency from the above converted values without applying indexation benefit.

Convert Capital gain into Indian currency: Capital Gains = Capital Gain in foreign currency × TT Buying rate on date of transfer

TAX ON DIVIDENDS, ROYALTY AND TECHNICAL SERVICE FEES IN THE CASE OF FOREIGN COMPANIES (SECTION 115A)

In case of a non-resident (not being a company) or of a foreign company, includes any income in the nature of:

- (a) Dividends other than dividends referred to in section 115-O will be taxable @ twenty per cent;
- (b) Interest received from Government or an Indian concern on monies borrowed or debt incurred by Government or the Indian concern in foreign currency [not being interest of the nature referred to in c or d below] will be taxable @ twenty per cent;
- (c) Interest received from an infrastructure debt fund referred to in clause (47) of section 10 will be taxable @ five per cent;

- (d) Interest of the nature and extent referred to in section 194LC (income by way of interest payable by the specified company) and interest of the nature and extent referred to in section 194LD (Income by way of interest on certain bonds and Government securities) will be taxable @ five per cent;
- (e) Income received in respect of units, purchased in foreign currency, of a Mutual Fund specified under clause (23D) of section 10 or of the Unit Trust of India will be taxable @ twenty per cent;
- (f) any income by way of royalty or fees for technical services (FTS) other than income referred to in section 44DA, received from Government or an Indian concern in pursuance of an agreement made by the foreign company with Government or the Indian concern (the agreement is approved by the Central Government or where it relates to a matter included in the industrial policy, for the time being in force, of the Government of India, the agreement is in accordance with that policy):

As per amendment by the Finance Act, 2013, with effect from 1.4.2014, above-mentioned royalty or FTS will be taxable at the rate of twenty five percent.

If royalty is received as consideration for transfer of all or any rights (including granting of licence) in respect of following, then approval of Central Government or conformity with Industrial Policy is not required if such books/computer software are permitted to be imported in India under Open General License:

- a. Copyrights in any book to an Indian concern or
- b. Any computer software to resident person

Deduction in respect of any expenditure or allowance shall not be allowed to the assessee under sections 28 to 44C and section 57 in computing his or its income referred to above.

Note:

1. Deduction under Chapter VI-A (Section 80C to 80U) shall not be allowed as deduction on interest or dividend income referred above.
2. It shall not be necessary for an assessee to furnish a return of his or its income if his or its total income during the previous year consisted only of income in the nature of dividend or interest referred above and the tax deductible at source under the provisions of Chapter XVII-B has been deducted from such income.

TAX ON INCOME FROM UNITS PURCHASED IN FOREIGN CURRENCY OR CAPITAL GAINS ARISING FROM THEIR TRANSFER (SECTION 115AB)

Income of an overseas financial organisation (hereinafter referred to as Offshore Fund) in respect of units purchased in foreign currency or income by way of long-term capital gains arising from the transfer of units purchased in foreign currency shall be taxable @ ten percent.

Deduction shall not be allowed to the assessee under sections 28 to 44C or clause (i) or clause (iii) of section 57 or under Chapter VI-A in respect of aforesaid income [and also indexation provisions shall not apply in respect of long term capital gains referred above];

Overseas financial organisation means any fund, institution, association or body, whether incorporated or not, established under the laws of a country outside India, which has entered into an arrangement for investment in India with any public sector bank or public financial institution or a mutual fund specified under clause (23D) of section 10 and such arrangement is approved by the Securities and Exchange Board of India.;

TAX ON INCOME FROM BONDS OR GLOBAL DEPOSITORY RECEIPTS PURCHASED IN FOREIGN CURRENCY OR CAPITAL GAINS ARISING FROM THEIR TRANSFER (SECTION 115AC)

Where a non-resident earns income by way of interest on bonds of an Indian company or on bonds of a public sector company sold by the Government, and purchased by him in foreign currency or income by way of dividends [other than dividends referred to in section 115-O] on Global Depository Receipts, or income by way of long-term capital gains arising from the transfer of bonds or Global Depository Receipts referred above, it will be taxable @ ten percent.

Deduction shall not be allowed to Non resident in respect of interest or dividends mentioned above, under sections 28 to 44C or under section 57 or under Chapter VI-A.

It shall not be necessary for a non-resident to furnish a return of his income if—

- (a) his total income in respect of which he is assessable under this Act during the previous year consisted only of interest or dividend income; and
- (b) the tax deductible at source under the provisions of Chapter XVII-B has been deducted from such income.

First and second provisos to section 48 shall not apply for the computation of long-term capital gains arising out of the transfer of long-term capital asset, being bonds or Global Depository Receipts referred above.

TAX ON INCOME FROM GLOBAL DEPOSITORY RECEIPTS PURCHASED IN FOREIGN CURRENCY OR CAPITAL GAINS ARISING FROM THEIR TRANSFER (SECTION 115ACA)

Where the total income of an individual, who is a resident and an employee of an Indian company engaged in specified knowledge based industry or service, or an employee of its subsidiary engaged in specified knowledge based industry or service (hereafter in this section referred to as the resident employee), includes:

- (a) income by way of dividends other than dividends referred to in section 115-O, on Global Depository Receipts of an Indian company engaged in specified knowledge based industry or service, issued in accordance with such Employees' Stock Option Scheme as the Central Government may, by notification in the Official Gazette, specify in this behalf and purchased by him in foreign currency: such income will be taxable @ ten percent; or
- (b) income by way of long-term capital gains arising from the transfer of Global Depository Receipts: such income will be taxable @ ten per cent;

Note:

1. Specified knowledge based industry or service means—
 - (i) information technology software;
 - (ii) information technology service;
 - (iii) entertainment service;
 - (iv) pharmaceutical industry;
 - (v) bio-technology industry; and

- (vi) any other industry or service, as may be specified by the Central Government, by notification in the Official Gazette;
- 2. Deduction shall not be allowed to him in respect of dividend income above, under any other provision of this Act;
- 3. First and second provisos to section 48 shall not apply for the computation of long-term capital gains arising out of the transfer of long-term capital asset, being Global Depository Receipts referred above.

TAX ON INCOME OF FOREIGN INSTITUTIONAL INVESTORS FROM SECURITIES OR CAPITAL GAINS ARISING FROM THEIR TRANSFER (SECTION 115AD)

Where a Foreign Institutional Investor earns:—

- (a) income other than income by way of dividends referred to in section 115-O received in respect of securities (other than units referred to in section 115AB): such income would be taxable @ twenty percent; or

However, the amount of income-tax calculated on the income by way of interest referred to in section 194LD shall be at the rate of five per cent;

Deduction under sections 28 to 44C or clause (i) or clause (iii) of section 57 or under Chapter VI-A shall not be allowed in respect of income referred above.

- (b) income by way of short-term or long-term capital gains arising from the transfer of such securities would be taxable @ thirty percent and ten percent respectively.

However, such short term capital gains referred to in Section 111A (i.e. on which securities transaction tax has been paid) shall be taxable @ fifteen percent.

First and second provisos to section 48 shall not apply for the computation of capital gains arising out of the transfer of securities referred above.

Note: Foreign Institutional Investor means such investor as the Central Government may, by notification in the Official Gazette, specify in this behalf.

TAX ON NON-RESIDENT SPORTSMEN OR SPORTS ASSOCIATIONS (SECTION 115BBA)

- (a) Income of a sportsman (including an athlete), who is not a citizen of India and is a non-resident, includes any income received or receivable by way of participation in India in any game (other than a game the winnings wherefrom are taxable under section 115BB) or sport or advertisement or contribution of articles relating to any game or sport in India in newspapers, magazines or journals, will be taxable @ twenty percent; or
- (b) Income of a non-resident sports association or institution, includes any amount guaranteed to be paid or payable to such association or institution in relation to any game (other than a game the winnings wherefrom are taxable under section 115BB) or sport played in India, will be taxable @ twenty percent; or
- (c) Income of an entertainer, who is not a citizen of India and is a non-resident, includes any income received or receivable from his performance in India, will be taxable @ twenty percent.

Deduction in respect of any expenditure or allowance shall not be allowed under any provision of this Act in computing the income referred to above.

It shall not be necessary for the assessee to furnish under sub-section (1) of section 139 a return of his income if his total income in respect of which he is assessable under this Act during the previous year consisted only of income referred above and the tax deductible at source under the provisions of Chapter XVII-B has been deducted from such income.

SPECIAL PROVISIONS RELATING TO CERTAIN INCOMES OF NON-RESIDENT INDIAN

Chapter XII-A containing 7 Sections from 115C to 115-I, contains special provisions relating to certain incomes of non-resident Indian. All these sections are given below:

DEFINITIONS (SECTION 115C)

- (a) Convertible Foreign Exchange means foreign exchange which is, for the time being, treated by the Reserve Bank of India as convertible foreign exchange for the purposes of the Foreign Exchange Management Act, 1999 and any Rules made thereunder.
- (b) Foreign Exchange Asset means any specified asset which the assessee has acquired, purchased with or subscribed to, in convertible foreign exchange.
- (c) Investment Income means any income other than dividend referred to in Section 115-O derived from a foreign exchange asset.
- (d) Long-term capital gains means income chargeable under the head "capital gains" relating to a capital asset being a foreign exchange asset which is not a short-term capital asset.
- (e) Non-resident Indian means an individual, being a citizen of India or a person of Indian origin who is not a resident. A person shall be deemed to be of Indian origin if he or either of his parents or any of his grandparents, was born in undivided India.
- (f) Specified Asset means any of the following assets:
 - (i) shares in an Indian company;
 - (ii) debentures issued by an Indian company which is not a private company as defined in the Companies Act, 1956;
 - (iii) deposits with an Indian company which is not a private company;
 - (iv) any security of the Central Government;
 - (v) such other assets as the Central Government may specify in this behalf by notification in the Official Gazette.

COMPUTATION OF INVESTMENT INCOME OF NON-RESIDENT (SECTION 115D)

No deduction in respect of any expenditure or allowance shall be allowed under any provisions of this Act in computing the investment income of a non-resident Indian -

In case of an assessee being a non-resident Indian -

- (a) if the gross total income consists only of investment income or income by way of long-term capital gains or both, no deductions shall be allowed to the assessee under chapter VI-A (Sections 80C to 80U) and nothing contained in the provisions of the second proviso to Section 48 shall apply to income chargeable under the head capital gains. (i.e. indexation benefit would not be available)

- (b) if the gross total income of such an assessee includes any income referred to under clause (a) above, the gross total income shall be reduced by the amount of such income and the deductions under chapter VI-A shall be allowed as if the gross total income as so reduced were the gross total income of the assessee.

TAX ON INVESTMENT INCOME AND LONG-TERM CAPITAL GAINS (SECTION 115E)

Where the total income of an assessee, being a non-resident Indian includes -

- (a) Income from foreign exchange asset (not applicable in the case of dividends referred to in section 115-O) @ 20%
- (b) Income by way of long term capital gains @10%

CAPITAL GAINS ON TRANSFER OF FOREIGN EXCHANGE ASSETS NOT TO BE CHARGED IN CERTAIN CASES (SECTION 115F)

In a case where a foreign exchange asset is transferred by the assessee and the net consideration for the transfer is invested by him within six months of the date of transfer in any specified asset or in notified savings certificates, any long-term capital gains arising from the transfer will not be charged to tax. If investment in the aforesaid specified assets or savings certificates is less than the net consideration, the exemption from tax in respect of the long-term capital gain will be allowed on proportionate basis.

It is also provided that if the new asset acquired by investing the net consideration realised on transfer of the foreign exchange asset is transferred or converted (otherwise than by transfer) into money, within three years from the date of acquisition, the amount of capital gains earlier exempted will be regarded as capital gains relating to long-term capital asset of the year in which the new asset is transferred or converted (otherwise than by transfer) into money.

'Net Consideration' in relation to the transfer of the original asset means the full value of the consideration received or accruing as a result of the transfer of such assets as reduced by any expenditure incurred wholly and exclusively in connection with such transfer.

RETURN OF INCOME NOT TO BE FILED IN CERTAIN CASES (SECTION 115G)

A non-resident Indian is not required to furnish his return of income u/s 139(1) if the following conditions are satisfied:

His total income in respect of which he is assessable under this Act during the previous year consists only of investment income or income by way of long-term capital gains or both and the tax at source has been deducted under the provisions of Chapter XVII-B.

BENEFIT UNDER THIS CHAPTER TO BE AVAILABLE IN CERTAIN CASES EVEN AFTER THE ASSESSEE BECOMES RESIDENT (SECTION 115H)

Where a person, who is a non-resident Indian in any previous year, becomes assessable as resident in India in respect of the total income of any subsequent year, he may furnish to the Assessing Officer a declaration in writing along with his return of income under section 139 for the assessment year for which he is so assessable, to the effect that the provisions of this Chapter shall continue to apply to him in relation to the investment income derived from any foreign exchange asset and if he does so, the provisions of Chapter XII-A shall continue to apply to him in relation to such income for that assessment year and for every subsequent assessment year until the transfer or conversion (otherwise than by transfer) into money of such assets.

In other words, in the case of a non-resident Indian who becomes resident in India in a subsequent year, the provisions of this Chapter XII-A will continue to apply in relation to the investment income derived from debentures of and deposits with an Indian public limited company and Central Government securities acquired in convertible foreign exchange, and other notified assets until the transfer or conversion (otherwise than by transfer) into money of such asset.

Chapter not to apply if the assessee so chooses (Section 115-I)

According to this section, a non-resident Indian will have the option or choice of not being assessed under the above provisions, for any assessment year by furnishing his return of income for that assessment year under Section 139, declaring therein his intention to that effect.

SELF-TEST QUESTIONS

These are meant for recapitulation only. Answers to the questions are not to be submitted for evaluation.

- (1) Explain the salient features of the tax incentives available to foreign institutional investors (FIIs) under the provisions of section 115AD of the Income-tax Act, 1961.
- (2) How the foreign institutional investors are taxed for the capital gains arising from transfer of securities?
- (3) Discuss, with the help of case law, if any, the taxability of the following incomes in case of a foreign company, assuming that the Indian subsidiary has no authority to enter into or conclude contracts on behalf of the foreign company:
 - (i) Income derived from back office operations performed by its Indian subsidiary;
 - (ii) Income from providing stewardship services to its Indian subsidiary involving briefing of the staff of the Indian company to ensure that the output meets the requirements of foreign company.
- (4) Compute the income tax: Royalty of ₹10 lakhs received by a foreign company from an Indian concern in pursuance of an agreement approved by the Central Government in the previous year 2013-14.

ANSWER/HINT:

- (3) Supreme Court in the case of DIT (International Taxation) v. Morgan Stanley & Co. Inc. (2007) 292 ITR 416.
- (4) ₹ 2.5 lakhs under Section 115A.

SUGGESTED READINGS

1. Girish Ahuja & Ravi Gupta : Professional Approach to Direct Taxes-Law and Practice
2. Dr. V K Singhania : Direct Taxes Law and Practices
3. B.B. Lal and N. Vashist : Direct Taxes, Income Tax, Wealth Tax and Tax Planning

INTERNATION TAXATION

PART II: ADVANCE RULING

In order to provide the facility of ascertaining the Income-tax liability of a non-resident, to plan their Income-tax affairs well in advance and to avoid long drawn and expensive litigation, a scheme of Advance Rulings has been introduced under the Income-tax Act, 1961. Authority for Advance Rulings has been constituted. A non-resident or certain categories of resident can obtain binding rulings from the Authority on question of law or fact arising out of any transaction/proposed transactions which are relevant for the determination of his tax liability.

After completion of this part, the student:

- will have the understanding of Advance Ruling Provisions
- will be aware about procedure for filing advance ruling application
- will be familiar with the constitution of Advance Ruling Authority.

CONCEPT OF ADVANCE RULING

The concept of advance rulings under the Act was introduced by the Finance Act, 1993, Chapter XIX-B of the Act, came into force with effect from 1.6.1993.

The term advance ruling has been defined in section 245N of the Act.

“Advance ruling” means,

- (i) a determination by the Authority in relation to a transaction which has been undertaken or is proposed to be undertaken by a non-resident applicant; or
- (ii) a determination by the Authority in relation to the tax liability of a non-resident arising out of a transaction which has been undertaken or is proposed to be undertaken by a resident applicant with such non-resident,
- (iii) a determination or decision by the Authority in respect of an issue relating to computation of total income which is pending before any income-tax authority or the Appellate Tribunal.

Further, advance ruling may be determined for both the question of law or fact.

WHO CAN SEEK ADVANCE RULING?

As per Section 245N(b) of the Income Tax Act, the advance ruling under the income-tax act could be sought by :

- (a) A non-resident;
- (b) Resident having transactions with non-residents.
- (c) Specified categories of residents.
 - I. A non-resident is defined in section 2(30) of the Income Tax Act as a person who is not a ‘resident’ and for the purposes of Section 92, 93 and 168, includes a person who is not ordinarily resident within the meaning of Clause 6 of Section 6.
 - II. A resident has been defined in section 2(42) of the Income Tax Act as a person who is resident in India within the meaning of Section 6.

III. A person has been defined in section 2(31) of the Income Tax Act as including :

- (i) an individual
- (ii) a Hindu undivided family
- (iii) a company
- (iv) a firm
- (v) an association of persons or a body of individuals, whether incorporated or not.
- (vi) a local authority; and
- (vii) every artificial juridical person, not falling within any of the preceding sub-clauses.

AUTHORITY FOR ADVANCE RULING (AAR) (SECTION 245O)

Under the scheme, the power of giving advance rulings has been entrusted to an independent adjudicatory body designated, as Authority for Advance Rulings (AAR). Accordingly, a high level body headed by a retired judge of the Supreme Court has been set-up. There are two members in the body. AAR is empowered to give rulings, which are binding both on the Income-tax Department and the applicant.

Constitution of AAR

AAR to consist of following members to be appointed by the Central Government:

- a Chairman, retired Judge of the Supreme Court
- an officer of the Indian Revenue Service who is qualified to be a member of CBDT
- an officer of the Indian Legal Service who is, or is qualified to be, an Additional secretary to the Government of India

AAR has been set up and is empowered to issue rulings which are binding both on the Income-tax Department and the applicant. This Authority is a quasi-judicial body having full powers of a civil court under the Income-tax Act to give its rulings in respect of specific questions of law or fact.

All the three Members of the Authority function as a body in disposing off the applications before them. However, section 245P makes it clear that no proceeding before the Authority, or the pronouncement of advance ruling by the Authority, shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the Constitution of the Authority.

Under Rule 27 of the AAR Procedure Rules, 1996 the proceedings of the Authority shall be conducted in the following manner:

- (1) When one or both of the members of the Authority other than Chairman is unable to discharge his functions owing to absence, illness or any other cause or in the event of occurrence of any vacancy or vacancies in the office of the members and the case cannot be adjourned for any reason, the Chairman alone or the Chairman and the remaining member may function as the Authority.
- (2) Subject to the provisions of sub-rule (3), in case there is difference of opinion among the members hearing an application, the opinion of the majority of members shall prevail and orders of the Authority shall be expressed in terms of the views of the majority but any member dissenting from the majority view may record his reasons separately.
- (3) Where the Chairman and one other member having a case under sub-rule (1) are divided in their opinions, the opinion of the Chairman shall prevail.

APPLICATION FOR ADVANCE RULING (SECTION 245Q)

An applicant shall make an application in such form and in such manner as may be prescribed, stating the question on which the advance ruling is sought. The application shall be made in quadruplicate and be accompanied by a fee of Ten thousand rupees. An applicant may withdraw an application within thirty days from the date of the application.

(a) FORMS

The application will be filed in the following Forms:

Form 34C: Applicable for a non-resident applicant.

Form 34D: Applicable for a resident having transactions with a non-resident

Form 34E: Applicable for the notified residents.

(b) PROCEDURE ON RECEIPT OF APPLICATION (SECTION 245R)

Inform CIT and call for records: On receipt of an application, the Authority shall forward one copy of the application to the Commissioner having jurisdiction over the case of the applicant and, if considered necessary by the Authority, relevant records can also be obtained from the Commissioner.

In cases where the applicants are not existing assesses, sometimes it becomes difficult to determine as to which Commissioner would have jurisdiction over the case of the applicant. In such cases, the Central Board of Direct Taxes (CBDT) is to be requested under Rule 13(1) of the Procedure Rules to designate a Commissioner in respect of an applicant within two weeks.

The designated Commissioner is also called upon to offer his comments on the contents of the application under Rule 13(2) of the Procedure Rules, which are considered by the Authority along with the statement of facts and submissions of the applicant.

Allowing or rejecting Application: Section 254R(2) of the Income Tax Act provides that the Authority may, after examining the application and the records called for, either 'allow' or 'reject' the application. The word 'allow' has been used synonymously with 'admit'. In other words, after examining the records, the Authority either admits or rejects the application. In case Authority has admitted the application, it is empowered to collect or receive additional material and it will examine all the material thus available to it at the time of hearing and pronouncing a ruling on the application. In case the application has been rejected, an opportunity of being heard must be given to the assessee.

AAR not to allow an application for Advance Ruling where the question raised in the application:

- (a) is already pending as on the date of application before any income tax authority or Appellate tribunal (except in case of public sector company);
- (b) is already pending as on the date of application before any court; or
- (c) involves determination of FMV of any property; or
- (d) relates to a transaction or issue, which is designed *prima facie* for avoidance of income tax (except in case of public sector company)

Issue to be pending in assessee's own case: Application will be rejected by AAR when the question raised in the application is pending in his own case before any income tax authority. An issue raised by any other person similar to the issue raised by the applicant in his application cannot disqualify the applicant's application.

For example, an issue raised by a payer of income in respect of liability towards TDS on the sum payable by the payer to the applicant, would not debar the applicant from raising issue before the AAR as to taxability of such payment in his hands. *[Ericsson telephone corporation India Ab. V. CIT (1997) 224 ITR 203(AAR)]*.

Allowance/Rejection Order to CIT and Applicant: The authority shall pass the ruling in writing within six months of the receipt of application and the copy of the order thereof, shall be sent to the commissioner and assessee.

Income tax authority or Appellate Tribunal shall not proceed to decide the issue if a resident applicant has made an application to AAR u/s 245Q in respect of any issue. [Section 245RR]

Appeal cannot be filed against the decision of the AAR. However, such ruling can be questioned by way of writ petition before the High Court, or by way of Special Leave Petition before the Supreme Court.

(c) SALIENT FEATURES

- (a) Available for Income-tax, Customs and Central Excise:

The benefit of advance ruling is available under the Income Tax Act, 1961, Central Excise Act, 1944 and Customs Act, 1962.

- (b) Must relate to a transaction entered into or proposed to be entered into by the applicant.

- (c) Questions on which ruling can be sought :

- (i) Even though the word used in the definition is singular namely “question”, it is clear that there can be more than one question in one application. This has been made amply clear by Column No.8 of the Form of application for obtaining an advance ruling (Form No.34C).
- (ii) a question can be both of law or fact, pertaining to the income tax liability of the non-resident qua the transaction undertaken or proposed to be undertaken.
- (iii) The questions may be on points of law as well as on facts or could be mixed questions of law and facts. There should be so drafted that each question is capable of an answer. This may need breaking-up of complex questions into two or more simple questions.
- (iv) The questions should arise out of the statement of facts given with the application. No ruling will be given on a purely hypothetical question. Question not specified in the application can be raised during the course of hearing. Normally a question is not allowed to be amended but in deserving cases AAR may allow amendment of one or more questions.
- (v) Subject to the limitations to be presently referred to, the question may relate to any aspect of the non-resident's liability including international aspects and aspects governed by double tax avoidance agreements. The questions may even cover aspects of allied laws that may have a bearing on tax liability such as the law of contracts, the law of trusts etc., but the question must have a direct bearing, on and nexus with the interpretation of the Indian Income-tax Act.

POWERS OF THE AUTHORITY (SECTION 245U)

Section 245U deals with the Powers of the Authority. Sub-section (1) provides that for the purpose of exercising its powers, the Authority shall have all the powers of a Civil Court under the Code of Civil Procedure, 1908 as are referred to in Section 131 of the Income-tax Act, when trying a suit in respect of the following matters, namely:

- (a) Discovery and inspection;
- (b) Enforcing the attendance of any person, including any officer of a banking company and examining him on oath;

- (c) Compelling the production of books of account and other documents; and
- (d) Issuing commissions.

Under sub-section (2) the Authority shall be deemed to be a Civil Court for the purposes of Section 195 of the Code of Criminal Procedure. Section 195 deals with 'Prosecution for contempt of lawful authority of public servants, for offences against public justice and for offences relating to documents given in evidence'. But it would not be deemed to be a Court for the purposes of Chapter XXVI of the Code of Criminal Procedure which deals with 'Provisions as to offences affecting the administration of justice'. Further, every proceeding before the authority shall be deemed to be a judicial proceeding within the meaning of Sections 193 and 228, and for the purpose of Section 196 of the Indian Penal Code.

APPLICABILITY OF ADVANCE RULING (SECTION 245S)

The advance ruling pronounced by the Authority under Section 245R shall be binding only :

- (a) On the applicant who had sought it;
- (b) In respect of the transactions in relation to which the ruling had been sought; and
- (c) On the Commissioner, and the income-tax authorities subordinate to him, in respect of the applicant and the said transaction.

The effect of the ruling is, understandably, stated to be confined to the applicant who has sought it as well as the Commissioner and the income-tax authority subordinate to him having jurisdiction over the case and that too only in relation to transaction for which advance ruling was sought. It may, however, be stated that the Authority generally follows the ruling in other cases on materially similar facts and, most certainly in other cases raising the same question of law, if any, which it has decided. The rule here is different from the position in other countries where either the taxpayer or the revenue or both are at liberty to accept the ruling or not.

Advance ruling not binding if there is a change in law or facts on the basis of which the advance ruling was pronounced.

QUESTION PRECLUDED

Under Section 254R, certain restrictions have been imposed on the admissibility of an application, if the question concerned is pending before other authorities. According to it, the authority shall not allow an application where the question raised by the non-resident applicant (or a resident applicant having transaction with a non-resident) is already pending before any income-tax authority or appellate tribunal or any court of law. However, exception has been provided in cases of resident applicants falling in sub-clause (iii) of Clause (b) of Section 245N in cases of pending before income tax authorities or the Tribunal. Further, the authority shall not allow the application where the question raised in it:

- (i) Involves determination of fair market value of any property; or
- (ii) It relates to a transaction or issue which is designed *prima facie* for the avoidance of income-tax.

ADVANCE RULING TO BE VOID [SECTION 245T]

Advance Ruling pronounced under section 245R will be void *ab initio* if:

- (a) the AAR finds on a representation made to it by Commissioner or otherwise that an advance ruling has been obtained by the applicant by fraud or misrepresentation of facts; and
- (b) the AAR by an order declares such advance ruling to be void *ab initio*.

Once an order declaring an advance ruling void is passed, all the provisions of the Act shall apply to the applicant as if advance ruling has not been made. A copy of such order shall be sent to the applicant and the CIT.

SELF-TEST QUESTIONS

These are meant for recapitulation only. Answers to the questions are not to be submitted for evaluation.

1. What is the procedure for making an application for obtaining advance rulings under section 245Q of the Income-tax Act, 1961?
 2. Explain the binding nature of advance ruling under the Income-tax Act, 1961.
 3. Can a resident assessee claim that the advance ruling obtained by his brother in respect of a similar issue faced by him is applicable to him also? Will such a ruling be binding on him also?
 4. Explain the powers of the authority for advance rulings in regard to rejection of an application and modification of an order.
 5. Discuss the procedure for filing application for advance ruling. Also, indicate the parties affected by the advance ruling.
 6. Whether tax is required to be deducted from commission paid to an agent outside India, if no services are performed in India or there is no fixed place of business in India? Explain and comment in the light of recent judgement of Authority for Advance Rulings (AAR).

Answer/Hint

3. No, advance ruling is binding only in the case of applicant.
 6. No tax is required to be deducted [AAR No. 802 of 2009]

SUGGESTED READINGS

1. Girish Ahuja & Ravi Gupta : Professional Approach to Direct Taxes-Law and Practice
 2. Dr. V K Singhania : Direct Taxes Law and Practices
 3. B.B. Lal and N. Vashist : Direct Taxes, Income Tax, Wealth Tax and Tax Planning

INTERNATION TAXATION

PART III: TRANSFER PRICING

After completion of this part, the student will

- understand the provisions of Transfer Pricing
- be familiar with concepts of International transaction, Associated Enterprise, Arm's Length Price, Documentations etc.
- be aware of the Methods for calculation of Arm's Length Price.

INTRODUCTION

In the present age of globalization, diversification and expansion, most of the companies are working under the umbrella of group engaged in diversified fields/sectors leading to large number of transactions between related parties.

Related Party transaction means the transaction between/among the parties which are associated by reason of common control, common ownership or other common interest.

The mechanism for accounting, the pricing for these related transactions is called Transfer Pricing.

Transfer Price refers to the price of goods/services which is used in accounting for transfer of goods or services from one responsibility centre to another or from one company to another associated company. Transfer price affect the revenue of transferring division and the cost of receiving division. As a result, the profitability, return on investment and managerial performance evaluation of both divisions are also affected.

This may be understood well by the following example

1. AT & Companies is a group of Companies engaged in diversified business. One of its units i.e. Unit X is engaged in manufacturing of automotive batteries. Another Unit Y is engaged in manufacturing of Industrial Trucks. Unit X is supplying automotive batteries to Unit Y. In such cases transfer price mechanism is used to account for the transfer of automotive batteries.
2. AT Co. is expert in providing electrical and electronic services. It is engaged in providing support to its associated company as well as it is engaged in outsourcing contract. If AT Co. provides some services to its associated company, the transaction should be accounted at price calculated using transfer price mechanism.

IMPORTANCE OF TRANSFER PRICING

Transfer pricing mechanism is very important for following reasons:

1. Helpful in correct pricing of Product/Services - An effective transfer pricing mechanism helps an organization in correctly pricing its product and services. Since in any organization, transaction between associated parties occurs frequently, it is necessary to value all transaction correctly so that the final product/ services may be priced correctly.
2. Helpful in Performance Evaluation: For the performance evaluation of any entity, it is necessary that all economic transactions are accounted. Calculation of correct transfer price is necessary for accounting of inter related transaction between two Associated enterprises.
3. Helpful in complying Statutory Legislations : Since related party transaction have a direct bearing on the profitability or cost of a company, the effective transfer pricing mechanism is very necessary.

For example, if the related party transactions are measured at less value, one unit may incur loss and other unit may earn undue profit. This will result in income tax imbalances at both parties end. Similarly, wrong transfer pricing may lead to wrong payment of excise duty, custom duty /sales tax (if applicable) as well.

TRANSFER PRICING PROVISIONS IN INDIA

Increasing participation of multi-national groups in economic activities in India has given rise to new and complex issues emerging from transactions entered into between two or more enterprises belonging to the same group. Hence, there was a need to introduce a uniform and internationally accepted mechanism of determining reasonable, fair and equitable profits and taxes in India. Accordingly, the Finance Act, 2001 introduced law of transfer pricing in India through Sections 92 to 92F of the Income Tax Act, 1961 which guides computation of the transfer price and suggests detailed documentation procedures. Year 2012 brought a big change in transfer pricing regulations in India whereby government extended the applicability of transfer pricing regulations to specified domestic transactions which are enumerated in Section 92BA. This would help in curbing the practice of transferring profit from a taxable domestic zone to tax free domestic zone.

As stated earlier, the fundamental of transfer pricing provision is that transfer price should represent the arm's length price of goods transferred and services rendered from one unit to another unit.

WHAT IS ARM'S LENGTH PRICE?

In general arm's length price means fair price of goods transferred or services rendered. In other words, the transfer price should represent the price which could be charged from an independent party in uncontrolled conditions. Arm's length price calculation is very important for a company. In case the transfer price is not at arm's length, it may have following consequences

- A. Wrong performance evaluation
- B. Wrong pricing of final product (In case where the goods/services are used in the manufacturing of final product)
- C. Non compliances of applicable laws and thus attraction of penalty provisions.

The same may be explained with the following examples

Company A and Company T is working under the common umbrella of AT & Company. Company A manufactures a product which is raw material for Company Y.

Case	Criteria	Effect on Company A	Effect on Company T
1	Company A charges price more than the Arm's length price from Company T	The revenue of company A will increase.	The total cost of company T will increase. This will result into wrong pricing of its product which may further lead to uncompetitiveness of its product
2	Company A charges price less than the Arm's length price from Company T	The revenue of company a will decrease. The parent company may close the company A treating it as loss making entity.	The total cost of company T will decrease. Therefore, the company B may charge lower price which may lead to loss at a group level.

3	Company A charges Arm's Length price from Company T	The revenue of company A will be representing true and fair view of its operation.	Company T will be paying the price as equivalent to market price of Company A product and its cost will be correct. On the basis of the cost arrived after considering the arm's length price of company A product, company T will be able to take correct price decision.
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"The concept of associated enterprises and International transaction are very important for applying the transfer pricing provisions. Section 92A and Section 92B deals with these two important concepts of chapter X of Income Tax Act, 1961."

ASSOCIATED ENTERPRISES (AE)

Associated Enterprises has been defined in Section 92A of the Act. It prescribes that "associated enterprise", in relation to another enterprise, means an enterprise—

- (a) Which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; or
- (b) In respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital, are the same persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise.

Thus, from above definition we may understand that

The basic criterion to determine an AE is the participation in management, control or capital (ownership) of one enterprise by another enterprise whereby the participation may be direct or indirect or through one or more intermediaries, control may be direct or indirect.

DEEMED ASSOCIATED ENTERPRISES

As per Section 92(2), two enterprises shall be deemed to be associated enterprises if, at any time during the previous year,—

- (a) one enterprise holds, directly or indirectly, shares carrying not less than twenty-six per cent of the voting power in the other enterprise; or
- (b) any person or enterprise holds, directly or indirectly, shares carrying not less than twenty-six per cent of the voting power in each of such enterprises; or
- (c) a loan advanced by one enterprise to the other enterprise constitutes not less than fifty-one per cent of the book value of the total assets of the other enterprise; or
- (d) one enterprise guarantees not less than ten per cent of the total borrowings of the other enterprise; or
- (e) more than half of the board of directors or members of the governing board, or one or more executive directors or executive members of the governing board of one enterprise, are appointed by the other enterprise; or
- (f) more than half of the directors or members of the governing board, or one or more of the executive directors or members of the governing board, of each of the two enterprises are appointed by the same person or persons; or

- (g) the manufacture or processing of goods or articles or business carried out by one enterprise is wholly dependent on the use of know-how, patents, copyrights, trade-marks, licences, franchises or any other business or commercial rights of similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model, design, secret formula or process, of which the other enterprise is the owner or in respect of which the other enterprise has exclusive rights; or
- (h) ninety per cent or more of the raw materials and consumables required for the manufacture or processing of goods or articles carried out by one enterprise, are supplied by the other enterprise, or by persons specified by the other enterprise, and the prices and other conditions relating to the supply are influenced by such other enterprise; or
- (i) the goods or articles manufactured or processed by one enterprise, are sold to the other enterprise or to persons specified by the other enterprise, and the prices and other conditions relating thereto are influenced by such other enterprise; or
- (j) where one enterprise is controlled by an individual, the other enterprise is also controlled by such individual or his relative or jointly by such individual and relative of such individual; or
- (k) where one enterprise is controlled by a Hindu undivided family, the other enterprise is controlled by a member of such Hindu undivided family or by a relative of a member of such Hindu undivided family or jointly by such member and his relative; or
- (l) where one enterprise is a firm, association of persons or body of individuals, the other enterprise holds not less than ten per cent interest in such firm, association of persons or body of individuals; or
- (m) there exists between the two enterprises, any relationship of mutual interest, as may be prescribed.

In Summary, two enterprises will be deemed as Associated Enterprises if

Quantum of Interest	Criteria applied for Associated Enterprises
26% or more	Shareholding with voting power – either direct or indirect
51% or more	Advancement of loan by one entity to other constituting certain percentage of the book value of the total assets of the other entity
51% or more	Based on the board of directors appointed by the governing board of the entity in the other
90% or more	Based on the quantum of supply of raw materials and consumables by one entity to the other
10% or more	Total Borrowing Guarantee by one enterprises for other
10% or more	Interest by a firm or association of Person(AOP) or by a body of Individual (BOI) in other firm AOP or firm or BOI

MEANING OF INTERNATIONAL TRANSACTION

International Transaction have been defined vide Section 92B of Income Tax Act. It provides that "International Transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

DEEMED INTERNATIONAL TRANSACTION

As per Section 92B(2) of Income Tax Act, A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of sub-section (1), be deemed to be a transaction entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise, or the terms of the relevant transaction are determined in substance between such other person and the associated enterprise.

Finance Act, 2012 has added an explanation for the purpose of Definition 92B and it provides that the expression "international transaction" shall include —

- (a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;
- (b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents, trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;
- (c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;
- (d) Provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;
- (e) A transaction of business restructuring or reorganization, entered into by an enterprise with an associated enterprise, irrespective of the fact that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date.

The term Intangible assets have also been elaborated and explanation to Section 92B provides that the expression Intangible shall include:

- (a) Marketing related intangible assets, such as, trademarks, trade names, brand names, logos;
- (b) Technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical know-how;
- (c) Artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;
- (d) Data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;
- (e) Engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schematics, blueprints, proprietary documentation;
- (f) Customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;
- (g) Contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements;
- (h) Human capital related intangible assets, such as, trained and organized work force, employment

- agreements, and union contracts;
- (i) Location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;
 - (j) Goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill of professional, celebrity goodwill, general business going concern value;
 - (k) Methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;
 - (l) Any other similar item that derives its value from its intellectual content rather than its physical attributes.'

The above explanation has added a wide range of Intangibles and the purpose of the explanation is to extend the applicability of Transfer pricing code to all International transaction involving the exchange of Intangibles which are not expressly available for trade .

TRANSFER PRICING – APPLICABILITY TO DOMESTIC TRANSACTIONS

Honourable Supreme court in the case of CIT v. Glaxo SmithKline Asia (P) Ltd., (2010) 195 Taxman 35 (SC) has advised that it needs to be considered whether the regulations should be applied to domestic transactions in cases where such transactions are not revenue-neutral. The facts and ruling of Honourable Supreme Court is following:

CIT v. Glaxo SmithKline Asia (P) Ltd., (2010) 195 Taxman 35 (SC)

Facts

1. Glaxo SmithKline Asia (P) Ltd (GSK) entered into an agreement with Glaxo Smith Kline Consumer Healthcare Ltd ("GSKCH") whereby GSKCH would provide all administrative services relating to marketing, finance, Human Resource (HR) to GSK for cost +5% markup.
2. The AO disallowed a part of the charges reimbursed on the ground that they were excessive and not for business purposes. On appeal by GSK, CIT (Appeals) upheld the decision of AO.
3. GSK appeal to Income Tax Appellate Tribunal (ITAT) and ITAT ruled that AO has no power to disallow any expenditure as excessive or unreasonable unless the case falls within the scope of Section 40A(2). The revenue appeal to high court and revenue appeal was dismissed by High court.
4. For subsequent years AO continued to follow the same approach and GSK continued to get relief from ITAT. Having regard to the delay on the part of revenue to give effect to ITAT order, GSK filed a writ petition before the High Court and High court issued direction to the Revenue to issue refund of taxes along with applicable interest.

Supreme Court Ruling

1. The revenue filed a Special Leave Petition (SLP) before the Honorable supreme court and supreme court held that since the exercise is revenue neutral and both the parties are not related parties in terms of Section 40A(2) of Income tax act, no interference is called for and the SLP filed by the Revenue is dismissed.
2. The honourable Supreme then stated that the larger issue is whether Transfer Pricing provisions should be limited to cross-border transactions or whether the Transfer Pricing Regulations be extended to domestic transactions. In domestic transactions, the under-invoicing of sales and over-invoicing of expenses ordinarily will be revenue neutral in nature, except in two circumstances

having tax arbitrage such as where one of the related entities is (i) loss making or (ii) liable to pay tax at a lower rate and the profits are shifted to such entity;

3. The Supreme court further held that the complications arise in cases where the fair market value is required to be assigned to transactions between related parties u/s 40A(2). The Central Board of Direct taxes (CBDT) should examine whether Transfer Pricing provisions can be applied to domestic transactions between related parties u/s 40A(2) by making amendments to the Act. The AO can be empowered to make adjustments to the income declared by the assessee having regard to the fair market value of the transactions between the related parties and can apply any of the generally accepted methods of determination of arm's length price, including the methods provided under Transfer Pricing provisions. The law can also be amended to make it compulsory for the taxpayer to maintain Books of Accounts and other documents on the lines prescribed in Rule 10D and obtain an audit report from his Chartered Accountant (CA) that proper documents are maintained;
4. Finally it was held that though the Court normally does not make recommendations or suggestions, in order to reduce litigation occurring in complicated matters, the question of extending Transfer Pricing regulations to domestic transactions require expeditious consideration by the Ministry of Finance and the CBDT may also consider issuing appropriate instructions in that regard.

SPECIFIED DOMESTIC TRANSACTIONS

Finance Act, 2012 has made a very important change and it has extended the applicability of Transfer Pricing Provisions to specified domestic transaction w.e.f. 1st April, 2012.

The specified domestic party transactions would essentially include payment made by a company to a related person referred to in Section 40A(2)(b) of the Act including payment to a director of the company or any person who has a substantial interest in the company (that is, has a beneficial ownership of shares carrying not less than 20 per cent of voting power); transactions referred to in Section 80A(6) of the Act (for example, transfer of goods or services from a tax-incentivised unit/entity to a non-tax-incentivised unit/entity and vice-versa); and transactions referred to in Section 80IA(8), 80IA(10) and 10AA(9) of the Act (carried out by industrial undertakings, infrastructure companies and units operating in special economic zones).

Section 92BA has been added in Transfer Price Code by Finance Act, 2012 which provides that

"Specified domestic transaction" in case of an assessee means any of the following transactions, not being an international transaction, namely:—

- (i) Any expenditure in respect of which payment has been made or is to be made to a person referred to in clause (b) of sub-section (2) of section 40A;
- (ii) Any transaction referred to in section 80A;
- (iii) Any transfer of goods or services referred to in sub-section (8) of section 80-IA;
- (iv) Any business transacted between the assessee and other person as referred to in sub-section (10) of section 80-IA;
- (v) Any transaction, referred to in any other section under Chapter VI-A or section 10AA, to which provisions of sub-section (8) or sub-section (10) of section 80-IA are applicable; or
- (vi) Any other transaction as may be prescribed,

and where the aggregate of such transactions entered into by the assessee in the previous year exceeds a sum of five crore rupees.'

Thus a specified domestic transaction means a transaction which is covered by criteria as given in section 92BA and the aggregate value of such transactions exceeds ₹5 crore in a year.

TRANSFER PRICING – METHODS

Section 92C of Income Tax Act defines the methods which are to be used in determination of Arm's Length prices for International Transaction and specified domestic transaction. The arm's length price in relation to an international transaction/specified domestic transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe, namely :-

- (A) Comparable Uncontrolled Price Method (CUP)
- (B) Resale Price Method (RPM)
- (C) Cost Plus Method (CPM)
- (D) Profit Split Method (PSM)
- (E) Transactional Net Margin Method (TNMM)
- (F) Such other method as may be prescribed by the Board.

Various transfer pricing methods which are prescribed by Income Tax Act, 1961 are as under:

(A) COMPARABLE UNCONTROLLED PRICE METHOD

Comparable Uncontrolled Price ("CUP") method compares the price charged for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances.

An Uncontrolled price is the price agreed between the unrelated parties for the transfer of goods or services. If this uncontrolled price is comparable with the price charged for transfer of goods or services between the Associated Enterprises, then that price is Comparable Uncontrolled Price (CUP). This is the most direct method for the determination of the Arms' length price.

Methods of CUP

CUP can be either

- (a) Internal CUP or
- (b) External CUP

Internal CUP is available, when the tax payer enters into a similar transaction with unrelated parties, as is done with a related party as well. This is considered a very good comparable, as the functions performed, processes involved, risks undertaken and assets employed are all easily comparable – more so, on "an apple to apple basis".

The external CUP is available if a transaction between two independent enterprises takes place under comparable conditions involving comparable goods or services. For example an independent enterprise buys or sells a similar product, in similar quantities under similar term from/to another independent enterprise in a similar market will be termed as external CUP.

Applicability of the CUP Method

Comparable Uncontrolled Price method is treated as most reliable method of transfer pricing calculation but

it is not easy to find the uncontrolled price. The CUP is believed to be the most reliable/best method, if one could identify and map it. CUP method can be applied without any difficulty in following circumstances.

- (1) Interest payment on a loan
- (2) Royalty payment
- (3) Software development where products are often licensed to a third party
- (4) Price charged for homogeneous items like traded goods

(B) RESALE PRICE METHOD

Rule 10B (1) (b) of Income Tax Rules, 1962 prescribes Resale Price method by which,

- A. The price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an unrelated enterprise is identified;
- B. Such resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions;
- C. The price so arrived at is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services;
- D. The price so arrived at is adjusted to take into account the functional and other differences, including differences in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market;
- E. The adjusted price arrived at under sub-clause (iv) is taken to be an arms length price in respect of the purchase of the property or obtaining of the services by the enterprise from the associated enterprise.

Example

1. A sold a machine to B (Associated enterprise) and in turn B sold the same machinery to C (an independent party) at sale margin of 30% for ₹2,10,000 but without making any additional expenses and charge. Here Arm's length price would be calculated as

$$\begin{aligned}
 \text{Sales price to B} &= ₹2, 10,000 \\
 \text{Gross Margin} &= ₹2,10,000 \times 30\% = ₹63,000 \\
 \text{Transfer price} &= ₹1, 47,000
 \end{aligned}$$

2. A sold a machine to B (Associated enterprise) and in turn B sold the same machinery to C (an independent party) at sale margin of 30% for ₹4,00,000 but B has incurred ₹4000 in sending the machine to C. Here Arm's length price would be calculated as

$$\begin{aligned}
 \text{Sales price to B} &= ₹4, 00,000 \\
 \text{Gross Margin} &= ₹4,00,000 \times 30\% = ₹1, 20,000 \\
 \text{Balance} &= ₹2, 80,000 \\
 \text{Less: Expenses incurred by B} &= ₹4,000 \\
 \text{Arm's length price} &= ₹2,76,000
 \end{aligned}$$

(C) COST PLUS METHOD

Rule 10B (1) (c) of Income tax Rules, 1962 prescribes Cost Plus Method, by which,

- (i) The direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an associated enterprise, are determined;
- (ii) The amount of a normal gross profit mark-up to such costs (computed according to the same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction, or a number of such transactions, is determined;
- (iii) The normal gross profit mark-up so determined is adjusted to take into account the functional and other differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market;
- (iv) The costs referred to in sub-clause (i) are increased by the adjusted profit mark-up arrived at under sub-clause (iii);
- (v) The sum so arrived at is taken to be an arm's length price in relation to the supply of the property or provision of services by the enterprise.

Under the Cost Plus Method, an arm's-length price equals the controlled party's cost of producing the tangible property plus an appropriate gross profit mark-up, defined as the ratio of gross profit to cost of goods sold (excluding operating expenses) for a comparable uncontrolled transaction.

The formulas for the transfer price in inter company transactions of products are as follows:

$$TP = COGS \times (1 + \text{mark-up})$$

Where:

- TP = Transfer Price of a product sold between a manufacturing company and a related company;
- COGS = Cost of goods sold of the manufacturing company
- Cost plus mark-up = gross profit mark-up defined as the ratio of gross profit to cost of goods sold

Gross profit is defined as sales minus cost of goods sold.

As an example, let us assume that the COGS in a transaction between two associated enterprises is ₹5,000. Assume that an arm's length gross profit mark-up that Associated Enterprise 1 should earn is 50%. The resulting transfer price between Associated Enterprise 1 and Associated Enterprise 2 is ₹ 7,500 [i.e. ₹5,000 × (1 + 0.50)].

In this method, calculation of cost of goods sold and gross margin are the most important factor.

(D) PROFIT SPLIT METHOD

Rule 10B (1) (d) of Income tax Rules, 1962 prescribes Profit Split Method, which may be applicable mainly in international transactions involving transfer of unique intangibles or in multiple international transactions which are so interrelated that they cannot be evaluated separately for the purpose of determining the arm's length price of any one transaction, by which:

- (i) The combined net profit of the associated enterprises arising from the international transaction in which they are engaged, is determined;

- (ii) The relative contribution made by each of the associated enterprises to the earning of such combined net profit, is then evaluated on the basis of the functions performed, assets employed or to be employed and risks assumed by each enterprise and on the basis of reliable external market data which indicates how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances;
- (iii) The combined net profit is then split amongst the enterprises in proportion to their relative contributions, as computed above;
- (iv) The profit thus apportioned to the assessee is taken into account to arrive at an arm's length price in relation to the international transaction.

However, the combined net profit as determined in sub-clause (i) may, in the first instance, be partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction in which it is engaged, with reference to market returns achieved for similar types of transactions by independent enterprises, and thereafter, the residual net profit remaining after such allocation may be split amongst the enterprises in proportion to their relative contribution in the manner specified under sub-clauses (ii) and (iii), and in such a case the aggregate of the net profit allocated to the enterprise in the first instance together with the residual net profit apportioned to that enterprise on the basis of its relative contribution shall be taken to be the net profit arising to that enterprise from the international transaction.

Two step Approach of Profit Spilt Method

Step 1: Allocation of sufficient profit to each enterprise to provide a basic compensation for routine contributions. This basic compensation does not include a return for possible valuable intangible assets owned by the associated enterprises. The basic compensation is determined based on the returns earned by comparable independent enterprises for comparable transactions or, more frequently, functions.

Step 2: Allocation of residual profit (i.e. profit remaining after step 1) between the associated enterprises based on the facts and circumstances. If the residual profit is attributable to intangible property, then the allocation of this profit should be based on the relative value of each enterprise's contributions of intangible property.

Example on the Profit Split Method (Residual Analysis Approach)

Company A is an Indian Company and deals in telecommunication products. It has developed a Microprocessor and it holds the patent for manufacturing of the microprocessor. Company B which is an overseas subsidiary of Company A is engaged in manufacturing of Mobile equipment at Australia. Company A supply the microprocessor to company B for using it in Mobile equipment and company B in turn after manufacturing the mobile sends the mobile to company "A" in India. Company A sells all the mobile in India.

Both companies contribute to the success of the mobile equipment through their design of the microprocessor and the equipment. As the nature of the products is very advanced and unique, the group is unable to locate any comparable with similar intangible assets. Therefore, neither the traditional methods i.e. CUP Method, RSP Method nor the TNMM is appropriate in this case.

Nevertheless, the group is able to obtain reliable data on hand phone contract manufacturers and equipment wholesalers without unique intangible property in the telecommunication industry. The manufacturers earn a mark-up of 10% while the wholesalers derive a 25% margin on sales.

Company A's and Company B's respective share of profit is determined in 2 steps using the profit split method (residual analysis approach).

Step 1 – Determining the basic return

The simplified accounts of Company A and Company B are shown below:

	Company B (₹ in Lakhs)	Company A (₹ in Lakhs)
Sales	100	125
Cost of Goods Sold	(60)	(100)
Gross Margin	40	25
Sales, General & Administration		
Expenses	(5)	(15)
Operating Margin	35	10

The total operating profit for the group is ₹45 Lakhs.

Company B

Particulars	Amount (₹ in Lakhs)
Cost of goods sold	60
Margin @10%	6
Transfer price based on Comparable (without considering Intangibles)	66

Company A

Particulars	Amount (₹ in Lakhs)
Sales to third party customers	125
Resale margin of wholesalers comparables (without intangibles)	
@25%	31.25
Gross Margin	31.25

	Company B (₹ in Lakhs)	Company A (₹ in Lakhs)
Sales	66	
Cost of Goods Sold	(60)	
Gross Margin	6	31.25
Sales, General & Admin Expenses	(5)	(15)
Routine operating margin	1	16.25

The total operating margin of the group is ₹17.25 Lakhs.

Step 2 : Dividing the residual profit

The residual profit of the group is = ₹45 Lakhs – ₹17.25 Lakhs = ₹27.75 Lakhs

On further study of the two companies, two particular expense items, R&D expenses and marketing expenses, are identified as the key intangibles critical to the success of the mobile equipment. The R&D expenses and marketing expenses incurred by each company are:

Company A	12 Lakhs (80%)
Company B	3 Lakhs (20%)

Assuming that the R&D and marketing expenses are equally significant in contributing to the residual profits, based on the proportionate expenses incurred:

Company A's share of residual profit ($80\% \times 27.75$)
= ₹22.20 Lakhs

Company B's share of residual profit ($20\% \times 27.75$)
= ₹5.55 Lakhs

Therefore, the adjusted operating profit of

Company A is = ₹22.20 L + ₹16.25 L = ₹38.45 Lakhs
Company B is = ₹5.55 + ₹1 = ₹6.55 Lakhs.

The adjusted tax accounts are as follows:

	<i>Company B</i> (₹ in Lakhs)	<i>Company A</i> (₹ in Lakhs)
Sales	71.55	125
Cost of Goods Sold	(60)	(71.55)
Gross Margin	11.55	53.45
Sales, General & Admin		
Expenses	(5)	(15)
Operating Margin	6.55	38.45

Hence, the transfer price determined using the profit split method (residual analysis approach) should be ₹71.55 Lakhs

(E) TRANSACTIONAL NET MARGIN METHOD (TNMM)

Rule 10B (1) (e) of Income Tax Rules, 1962 prescribes, Transactional net margin method, by which,

- (i) The net profit margin realized by the enterprise from an international transaction entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;
- (ii) The net profit margin realized by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;
- (iii) The net profit margin referred to in (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;
- (iv) the net profit margin realized by the enterprise and referred to in (i) is established to be the same as the net profit margin referred to in (iii);
- (v) The net profit margin thus established is then taken into account to arrive at an arms length price in relation to the international transaction.

Example

Nikhil & Co is an India manufacturer of dishwashers. All Nikhil & Co's dishwashers are sold to an overseas associated enterprise, Company G, and bears Company G's brand. Company G, a household electrical appliances brand name, sells only dishwashers manufactured by Nikhil & Co.

The CUP method is not applied in this case because no reliable adjustments can be made to account for differences with similar products in the market. After the appropriate functional analysis, Nikhil & Co was able to identify an Indian manufacturer of home electrical appliances, Company H, as a suitable comparable company. However, Company H performs warranty functions for its independent wholesalers, whereas Nikhil & Co does not. Company H realizes a net mark up (i.e. operating margin) of 10%.

As the costs pertaining to the warranty functions cannot be separately identified in Company H's accounts and no reliable adjustments can be made to account for the difference in the functions, it may be more reliable to examine the net margins in this case.

Solution

The transfer price for Nikhil & Co's sale of dishwashers to Company G is computed using the TNMM as follows:

Nikhil & Co's cost of goods sold	₹5,000
Nikhil & Co's operating expenses	₹1,500
Total costs	₹6,500
Add: Net mark up @ 10% (10% x 6,500)	₹ 650
Transfer price based on TNMM	₹7,150

SELECTION OF TRANSFER PRICING METHOD

Rule 10C of the Indian Income Tax Rules, 1962 states that:

In selecting a most appropriate method, the following factors shall be taken into account namely,

- The nature and class of the international transaction.
- The class or classes of Associated Enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enterprises.
- The availability, coverage and reliability of data necessary for application of the method.
- The degree of comparability existing between the international transaction and the uncontrolled transaction and between the enterprises entering into such transactions.
- The extent to which reliable and accurate adjustments can be made to account for differences, if any, between the international transaction and the comparable uncontrolled transactions or between the enterprises entering into such transactions.
- The nature, extent and reliability of assumptions required to be made in the application of a method.

The starting point to select the most appropriate method is the functional analysis which is necessary regardless of what transfer pricing method is selected. Each method may require a deeper analysis focusing on aspects relating to various methods. The functional analysis helps to:

- Identify and understand the intra-group transactions;
- Have a basis for comparability;
- Determine any necessary adjustments to the comparables;
- Check the accuracy of the method selected; and
- Over time, to consider adaptation of the policy if the functions, risks or assets have been modified.

Functional analysis also forms part of the documentation. The major components of a functional analysis are:

1. *Identification of Functions Performed : For the purpose of determining comparability, functions of the entities play an important role.*
2. *Identification of Risk Undertaken : A risk-bearing party should have a chance of higher earnings than a non-risk bearing party, and will incur the expenses and perhaps related loss if and when risk materializes.*
3. *Identification of Assets used or contributed : The functional analysis must identify and distinguish tangible assets and intangible assets as this is very important for functional analysis.*

The functional analysis provides answers to identify which functions risks and assets are attributable to the various related parties. In some cases one company may perform one function but the cost thereof is incurred/ paid by the other party to the transaction. The functional analysis could emphasize that situation. The functional analysis includes reference to the industry specifics, the contractual terms of the transaction, the economics circumstances and the business strategies. A checklist with columns for each related party and if needed for the comparable parties could be used to summarize the functional analysis and give a quick idea of which party performs each relevant function, uses what assets and bears which risk. But this short-cut overview should not be used by tax auditors to count the number of enumerated functions, risks and assets in order to determine the arm's length compensation. It should be used to consider the relative importance of each function, risk and asset. Once the functional analysis is performed and the functionality of the entity as regards the transactions subject to review (or the entity as a whole) has been completed, it can be determined what transfer pricing method is most suitable to determine the arm's length price for the transactions under the review (or the operating margin for the entity under review).

There is no universally accepted method or model which describes the technique for choosing a transfer pricing method. Traditionally comparable Uncontrolled Pricing Method, Profit Split Method, Resale Price Methods are being used in transfer pricing. Other method as TNMM may also be used after the functional analysis and global practices analysis.

REFERENCE TO TRANSFER PRICING OFFICER

Section 92CA of Income Tax Act deals with Reference to Transfer Pricing Officer by assessing officer.

It provides that Assessing Officer with prior approval of Commissioner may refer the computation of Arm's Length Price in an International Transaction to transfer pricing officer if he considers it necessary or expedient to do so. On reference by Assessing officer, Transfer Pricing Officer (TPO) shall serve a notice to the Assessee requiring him to produce the evidence in support of computation made by him of Arm's Length Price in relation to an International transaction

WHO IS TRANSFER PRICING OFFICER (TPO)

For the purpose of Section 92CA "Transfer Pricing Officer" means a Joint Commissioner or Deputy Commissioner or Assistant Commissioner authorized by the Board to perform all or any of the functions of an Assessing Officer specified in sections 92C and 92D in respect of any person or class of persons.

DETERMINATION OF ARM'S LENGTH PRICE BY TRANSFER PRICING OFFICER

Transfer Pricing Officer after hearing the evidences, information or documents as produced by assessee and after considering such evidence as he may require on any specified points and after taking into account all relevant materials which he has gathered, shall, by order in writing, determine the arm's length price in

relation to the international transaction/specified transaction and send a copy of his order to the Assessing Officer and to the assessee.

On receipt of the order from Transfer Pricing officer, the Assessing Officer shall proceed to compute the total income of the assessee in conformity with the arm's length price as determined by the Transfer Pricing Officer.

RECTIFICATION OF ARM'S LENGTH PRICE ORDER BY TRANSFER PRICING OFFICER

If any mistake is observed which is apparent from record, the Transfer Pricing Officer may amend any order passed by him and the provisions of Section 154 w.r.t. rectification of mistake shall apply accordingly. Where any amendment is made by the Transfer Pricing Officer, he shall send a copy of his order to the Assessing Officer who shall thereafter proceed to amend the order of assessment in conformity with such order of the Transfer Pricing Officer.

POWERS OF TRANSFER PRICING OFFICER

1. *Power to call evidences/Information from Assessee:*

As per Section 92CA(2), the Transfer Pricing Officer may issue a notice to the Assessee and ask him to furnish records, evidences, information in support of the computation of Arm's Length Price relating to the International Transaction.

2. *Power to amend the Order made in regard to computation of Arm length price for the transaction referred to him:*

As stated earlier, if any mistake is observed which is apparent from record, the Transfer Pricing Officer may amend any order passed by him and the provisions of section 154 w.r.t. rectification of mistake shall apply accordingly

3. *Power to proceed if the report under Section 92E is not furnished for some International transactions:*

Finance Act, 2012 has inserted section 92CA(2B) in the Act which provides that w.e.f. 1st June, 2002 if the assessee has not furnished Form 3CEB mentioned u/s 92E and the transfer pricing officer observe International transaction or specified domestic transactions during the course of the proceedings before him, he may proceed with deeming that such transaction has been referred to him under this section 92CA provided that the provision of this section shall not empower the Assessing Officer either to assess or reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year, proceedings for which have been completed before the 1st day of July, 2012

4. *Power to proceed into the cases not referred to him:*

As per amendment made by Finance Act, 2011 the jurisdiction of the Transfer Pricing Officer shall extend to the determination of the Arm's Length Price (ALP) in respect of other international transactions which are noticed by him subsequently, in the course of proceedings before him. These international transactions would be in addition to the international transactions referred to the TPO by the Assessing Officer

5. *Power to exercise all of the following powers specified in Sections 131(1)(a) to 131(1)(d) or 133(6) or 133A of Income Tax Act:*

Power u/s 131(1)(a) to 131(1)(d)

TPO have the same powers as are vested in a Court under the Code of Civil Procedure, 1908 (5 of

1908), when trying a suit in respect of the following matters, namely:—

- (a) discovery and inspection;
- (b) enforcing the attendance of any person, including any officer of a banking company and examining him on oath;
- (c) compelling the production of books of account and other documents; and
- (d) Issuing commissions.

Power u/s 133(6)

Under Section 133(6), TPO may require any person, including a banking company or any officer thereof, to furnish information in relation to such points or matters, or to furnish statements of accounts and affairs verified in the manner specified by him giving information in relation to such points or matters as his opinion will be useful for, or relevant to, any enquiry or proceeding under this Act.

Power u/s 133A - Power of Survey

Finance Act, 2011 has made an amendment which provides for the power of Survey to TPO through introduction of Section 133A. In course of the proceedings, a TPO may carry out the survey as per section 133A of Income Tax Act.

ADVANCE PRICING AGREEMENT

As per Section 92CC of Income Tax Act, 1961, w.e.f. 1st July, 2012, the Central Board of Direct Taxes (Board), with the approval of the Central Government, may enter into an Advance Price Agreement with any person, determining the arm's length price or specifying the manner in which arm's length price is to be determined, in relation to an international transaction to be entered into by that person.

Advance Pricing Agreement (APA) is an agreement between a taxpayer and a taxing authority (Board) on an appropriate transfer pricing methodology for fixing the arm's length price for a set of transactions over a fixed period of time in future. Importance of APA may be understood with the fact that in financial year 2011-2012, addition of about ₹40,000 crore income has been proposed by Transfer pricing officers.

CALCULATION OF ARM'S LENGTH PRICE UNDER ADVANCE PRICING AGREEMENT

Arm's Length Price under Advance Pricing Agreement shall be calculated as per method enumerated in section 92C (1) or any other method with such adjustment and variation as may be necessary and expedient so to do.

Section 92C (1) of Income Tax Act prescribes that the arm's length price in relation to an international transaction shall be determined by any of the following methods, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or functions performed by such persons or such other relevant factors as the Board may prescribe (see rule 10B) namely:—

- (a) Comparable uncontrolled price method;
- (b) Resale price method;
- (c) Cost plus method;
- (d) Profit split method;
- (e) Transactional net margin method;

- (f) Such other method as may be prescribed by the Board.

Notwithstanding anything contained in Section 92C or Section 92CA, if the Advance Pricing Agreement has been entered between an assessee and Board in respect of one international transaction, the arm's length price will be calculated as per the provisions of Advance Pricing Agreement.

VALIDITY OF ADVANCE PRICING AGREEMENT

The Advance Pricing Agreement shall be valid for a period as specified in the Advance Pricing Agreement. However, this period will not be more than 5 consecutive years.

BINDINGNESS OF ADVANCE PRICING AGREEMENT

Advance Pricing Agreement shall be binding on:

- (a) the person in whose case, and in respect of the transaction in relation to which, the agreement has been entered into; and
- (b) on the Commissioner, and the income-tax authorities subordinate to him, in respect of the said person and the said transaction

However the advance pricing agreement shall not be binding if there is a change in law or facts having bearing on the agreement so entered.

DECLARING AN ADVANCE PRICING AGREEMENT VOID AB INITIO

The Board may, with the approval of the Central Government, by an order, declare an agreement to be void ab initio, if it finds that the agreement has been obtained by the person by fraud or misrepresentation of facts.

EFFECT OF DECLARING AN ADVANCE PRICING AGREEMENT VOID AB INITIO

If an agreement is declared void ab initio —

- (a) All the provisions of the Act shall apply to the person as if such agreement had never been entered into; and
- (b) Notwithstanding anything contained in the Act, for the purpose of computing any period of limitation under this Act, the period beginning with the date of such agreement and ending on the date of order for declaring an Advance Pricing Agreement void ab initio shall be excluded. Provided that where immediately after the exclusion of the aforesaid period, the period of limitation, referred to in any provision of this Act, is less than sixty days, such remaining period shall be extended to sixty days and the aforesaid period of limitation shall be deemed to be extended accordingly.

PROCEDURE AND SCHEME OF ADVANCE PRICING AGREEMENT

The Board may, for the purposes of this section, prescribe a scheme specifying therein the manner, form, procedure and any other matter generally in respect of the Advance Pricing Agreement. Where an application is made by a person for entering into Advance Pricing Agreement, the proceeding shall be deemed to be pending in the case of the person for the purposes of the Act.

FILING OF MODIFIED RETURN FOR ANY ASSESSMENT YEAR RELEVANT TO A PREVIOUS YEAR TO WHICH APA APPLIES

As per Section 92CD of Income Tax Act, 1961, w.e.f. 1st July, 2012 notwithstanding anything to the

contrary contained in Section 139, where any person has entered into an agreement and prior to the date of entering into the agreement, any return of income has been furnished under the provisions of Section 139 for any assessment year relevant to a previous year to which such agreement applies, such person shall furnish, within a period of three months from the end of the month in which the said agreement was entered into, a modified return in accordance with and limited to the agreement. Save as otherwise provided in Section 92CD, if modified return is furnished under Section 139, all other provision of the Act shall apply accordingly.

Thus, Section 92CD provides an opportunity to taxpayer to avoid the litigation even for the years for which return has already been filed.

Reassessment of Total Income in the cases where Modified return has been filed but the Assessment/Reassessment proceedings have been completed before the expiry of period allowed for furnishing of modified return

As per Section 92CD(3), if the assessment or reassessment proceedings for an assessment year relevant to a previous year to which the agreement applies have been completed before the expiry of period allowed for furnishing of modified return under Section 92CD , the Assessing Officer shall, in a case where modified return is filed under this Section, proceed to assess or reassess or recompute the total income of the relevant assessment year having regard to and in accordance with the agreement.

Application of APA in the pending assessment or reassessment for an assessment year relevant to the previous year to which the agreement applies and modified return has been filed under Section 92 CD.

Where the assessment or reassessment proceedings for an assessment year relevant to the previous year to which the agreement applies are pending on the date of filing of modified return in accordance with the provisions of sub-section (1), the Assessing Officer shall proceed to complete the assessment or reassessment proceedings in accordance with the agreement taking into consideration the modified return so furnished.

Extension of Limitation Period in the cases where modified return is filed under Section 92CD

As per Section 92CD (5), notwithstanding anything contained in Section 153 or Section 153B or Section 144C—

- (a) The order of assessment, reassessment or recomputation of total income under Section 92CD (3) shall be passed within a period of one year from the end of the financial year in which the modified return under sub-section (1) is furnished;
- (b) The period of limitation as provided in Section 153 or Section 153B or Section 144C for completion of pending assessment or reassessment proceedings referred to Section 92CD(4) shall be extended by a period of twelve months.

This may be observed from above provision that Advance Pricing Agreement, although styled as "advance" agreements, may be a good arm in the resolution of transfer pricing issues pending from prior years—and in some cases it can provide an effective means for resolving existing transfer pricing audits or adjustments.

By virtue of Advance Pricing Agreement, the taxpayer is assured about the Tax Liability arising out of International transaction. No surprises or challenges will arise if the agreement is followed. The scope of certainty includes tax treatment of covered transactions as to amount and characterization, elimination of potential penalties for substantial tax understatement and a limitation of record-keeping requirements.

TRANSFER PRICING – DOCUMENTATION

The legal framework for maintenance of information and documentation by a taxpayer is provided in Section 92D of Income Tax Act, 1961 which lays down that every person who enters into an international transaction with an associated enterprise shall maintain prescribed information and documents.

The various types of information and documents to be maintained in respect of an international transaction, the associated enterprise and the transfer pricing method used are prescribed in Rule 10D of the Income Tax Rules, as under:

- (a) A description of the ownership structure of the enterprise and details of shares or other ownership interest held therein by other enterprises;
- (b) A profile of the multinational group of which the assessee enterprises i.e. taxpayer is a part and the name, address, legal status and country of tax residence of each of the enterprises comprised in the group with whom international transactions have been made by the taxpayer and the ownership linkages among them;
- (c) A broad description of the business of the taxpayer and the industry in which it operates and the business of the associated enterprises;
- (d) The nature, terms and prices of international transaction entered into with each associated enterprise, details of property transferred or services provided and the quantum and the value of each such transaction or class of such transaction;
- (e) A description of the functions performed, risks assumed and assets employed or to be employed by the taxpayer and by the associated enterprise involved in the international transaction;
- (f) A record of the economic and market analysis, forecasts, budgets or any other financial estimates prepared by the taxpayer for its business as a whole or separately for each division or product which may have a bearing on the international transaction entered into by the taxpayer;
- (g) A record of uncontrolled transactions taken into account for analysing their comparability with the international transaction entered into, including a record of the nature, terms and conditions relating to any uncontrolled transaction with third parties which may be relevant to the pricing of the international transactions;
- (h) A record of the analysis performed to evaluate comparability of uncontrolled transactions with the relevant international transaction;
- (i) A description of the methods considered for determining the arm's length price in relation to each international transaction or class of transaction, the method selected as the most appropriate method along with explanations as to why such method was so selected, and how such method was applied in each case;
- (j) A record of the actual working carried out for determining the arm's length price, including details of the comparable data and financial information used in applying the most appropriate method and adjustments, if any, which were made to account for differences between the international transaction and the comparable uncontrolled transactions or between the enterprises entering into such transaction;
- (k) The assumptions, policies and price negotiations if any which have critically affected the determination of the arm's length price;
- (l) Details of the adjustments, if any made to the transfer price to align it with arm's length price determined under these rules and consequent adjustment made to the total income for tax purposes;

- (m) Any other information, data or document, including information or data relating to the associated enterprise, which may be relevant for determination of the arm's length price.

Rule 10D also prescribes that the above information is to be supported by authentic documents which may include the following:

- (a) Official publications, reports, studies and data bases of the government of the country of residence of the associated enterprise or of any other country;
- (b) Reports of market research studies carried out and technical publications of institutions of national or international repute;
- (c) Publications relating to prices including stock exchange and commodity market quotations;
- (d) Published accounts and financial statements relating to the business of the associated enterprises;
- (e) Agreements and contracts entered into with associated enterprises or with unrelated enterprises in respect of transaction similar to the international transactions;
- (f) Letters and other correspondence documenting terms negotiated between the taxpayer and associated enterprise;
- (g) Documents normally issued in connection with various transaction under the accounting practices followed.

BURDEN OF PROOF

It is noteworthy that the information and documentation requirements referred to above are linked to the burden of proof laid on the taxpayer to prove that the transfer price adopted is in accordance with the arm's length principle. One of the conditions to be fulfilled for discharging this burden by the taxpayer is maintenance of prescribed information and documents in respect of an international transaction entered into with a associated enterprise. A default in maintaining information and documents in accordance with the rules is one of the conditions which may trigger a transfer pricing audit under Section 92C(3). Any default in respect of the documentation requirement may also attract penalty of a sum equal to two percent of the value of the international transaction (Sec 271AA).

SUBMISSION OF DOCUMENTS WITH THE TAX AUTHORITIES

There is no reference in the provisions included either in the Income Tax Act or the Income Tax Rules about any requirement to submit the prescribed information and documents at the stage of initial compliance in the form of submission of report under Section 92E. All that Section 92E requires is that the concerned taxpayer shall obtain a Report from an Accountant in the prescribed form (Form 3CEB) and submit the Report by the specified date.

Form 3CEB contains a certificate from the Accountant that in his opinion proper information and documents as prescribed have been maintained by the taxpayer. Rule 10D requires that the information and document maintained should be contemporaneous as far as possible and should exist latest by the specified date for filing the report under Section 92E. Section 92D also provides that information and documentation may be requisitioned by the Assessing Officer or the Appellate Commissioner on a notice of thirty days which period may be extended by another period of 30 days.

NON APPLICABILITY OF DOCUMENTATION REQUIREMENT

Although the law has prescribed no monetary limit in respect of international transaction covered by the transfer pricing requirements, an exception is provided in para 2 of Rule 10D in respect of the maintenance of information and document requirement in respect of international transactions not exceeding ₹100 Lakhs . It is provided that the above requirement will not apply to such transactions. However, the concerned taxpayer may be required to substantiate on the basis of available material that the income arising from the international transaction is computed in accordance with the arm's length rule.

RETENTION PERIOD OF DOCUMENTS KEPT UNDER RULE 10D

The prescribed information and documents are required to be maintained for a period of six years from the end of the relevant Assessment years thus the information and documents are required to be maintained for a period of eight years. Rule 10D absolves a taxpayer entering into an international transaction which continues to have effect over more than one year from maintaining separate set of documents for each year. However separate documents are required for each year if there is any significant change in the terms and conditions of the international transaction which have a bearing on the transfer price.

TRANSFER PRICING – PENALTY FOR CONTRAVENTION

Contravention of Transfer Pricing provisions as contained in Chapter X of the Income tax Act, 1961 may invite hefty penalties. The details of penalties under different sections of Income tax Act, 1961 are as follows:-

A. Penalty for concealment of income or for furnishing inaccurate particulars of such income under Section 271(1)(c)

If the Assessing Officer or Commissioner (Appeals) or the Commissioner in the course of any proceedings under this Act, is satisfied that any person has concealed the particulars of his income or furnished inaccurate particulars of such income, he may direct that such person shall pay by way of penalty in addition to tax, if any, payable by him, a sum which shall not be less than, but which shall not exceed three times, the amount of tax sought to be evaded by reason of the concealment of particulars of his income or the furnishing of inaccurate particulars of such income.

Explanation 7 to Section 271(1)(c) - Where in the case of an assessee who has entered into an international transaction defined in section 92B, any amount is added or disallowed in computing the total income under sub-section (4) of section 92C, then, the amount so added or disallowed shall, for the purposes of clause (c) of this sub-section, be deemed to represent the income in respect of which particulars have been concealed or inaccurate particulars have been furnished, unless the assessee proves to the satisfaction of the Assessing Officer or the Commissioner (Appeals) or the Commissioner that the price charged or paid in such transaction was computed in accordance with the provisions contained in section 92C and in the manner prescribed under that Section, in good faith and with due diligence.

B. Penalty for failure to furnish information or document - Section 271G

As per Section 271G of Income Tax Act, If any person who has entered into an international transaction fails to furnish any such information or document as required by sub-section (3) of section 92D, the Assessing Officer or the Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to two per cent of the value of the international transaction for each such failure.

C. Penalty for failure to keep and maintain information and document in respect of International transaction - Section 271AA

Without prejudice to the provisions of Section 271 or Section 271BA, if any person in respect of an International transaction fails to keep and maintain any such information and document as required by sub-section (1) or sub-section (2) of Section 92D, the Assessing Officer or Commissioner (Appeals) may direct that such person shall pay, by way of penalty, a sum equal to two per cent of the value of each international transaction entered into by such person.

D. Penalty for failure to furnish report under Section 92E - Section 271BA

If any person fails to furnish a report from an accountant as required by Section 92E, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of one hundred thousand rupees.

E. Penalty for failure to answer questions, sign statements, furnish information, returns or statements etc. - Section 272A

If any person,—

- (a) being legally bound to state the truth of any matter touching the subject of his assessment, refuses to answer any question put to him by an income-tax authority in the exercise of its powers under this Act; or
- (b) refuses to sign any statement made by him in the course of any proceedings under this Act, which an income-tax authority may legally require him to sign; or
- (c) to whom a summons is issued under sub-section (1) of Section 131 either to attend to give evidence or produce books of account or other documents at a certain place and time omits to attend or produce books of account or documents at the place or time, he shall pay, by way of penalty, a sum of ten thousand rupees for each such default or failure.

SELF-TEST QUESTIONS

These are meant for recapitulation only. Answer to the questions are not to be submitted for evaluation.

1. What is the role of Transfer Pricing Officer? Is it possible for the Assessing Officer to pass the assessment order pertaining to the Assessment Year 2014-15 without considering arm's length price determined by the Transfer Pricing Officer?
2. Explain, with the help of a simple example, the determination of arm's length price where more than one such price is arrived at by the Transfer Pricing Officer by following the most appropriate method.
3. Explain how the arm's length price in relation to an international transaction is computed under the comparable uncontrolled price method as per Rule 10B of the Income-tax Rules, 1962.
4. What is the time limit for completion of assessment in case reference is made to Transfer Pricing officer?
5. What is Transfer Price? Briefly state the importance of Transfer Pricing System.
6. Why do transfer pricing systems exist? What are the criteria to be considered in assessing a system of transfer pricing?
7. Compute the arm's length price (ALP) in the following cases:
 - (a) Medical Instruments Ltd. is a 100% Indian subsidiary of a US company. The parent company sells one of its products to the Indian subsidiary at a price of US \$ 100 per unit. The same product is sold to unrelated buyers in India at a price of US \$ 125 per unit.
 - (b) The US parent company sells the same product to an unrelated company in India @ US \$ 80 per unit.

Answer/Hint:

7. (a) ALP = \$ 125 per unit, but transfer pricing provision will not apply as by applying ALP, there will be reduction in taxable income in India; (b) ALP = \$ 80 per unit

Suggested Readings

1. Girish Ahuja & Ravi Gupta : Professional Approach to Direct Taxes-Law and Practice
2. Dr. V K Singhania : Direct Taxes Law and Practices
3. B.B. Lal and N. Vashist : Direct Taxes, Income Tax, Wealth Tax and Tax Planning

INTERNATION TAXATION

PART IV: DOUBLE TAXATION AVOIDANCE AGREEMENTS

After completion of this lesson, student will

- have the understanding of double taxation provisions.
- Know how to avail the benefit of tax treaties.
- Know how to take the rebate where unilateral agreement is there.

The situation of double taxation will arise where the income gets taxed in two or more than two countries whether due to residency or source principle as the case may be. The problem of double taxation arises if the income of a person is taxed in one country on the basis of residence and on the basis of residency in another country or on the basis of both. To mitigate the double taxation of income the provisions of double taxation relief were made. The double taxation relief is available in two ways one is unilateral relief and other is bilateral relief.

Government of India can enter into agreement with a foreign government vide Entry 14 of the Union List regarding any matter provided Parliament verifies it. Double Tax Avoidance Agreement is a kind of bilateral treaty or agreement, between Government of India and any other foreign country or specified territory outside India. Such treaty or agreement is permissible in terms of Article 253 of the Constitution of India.

AGREEMENTS WITH FOREIGN COUNTRIES OR SPECIFIED TERRITORIES (SECTION 90)

India has entered into bilateral agreements with many countries regarding avoidance of double taxation including tax avoidance and tax evasion issues. Section 90 of the income Tax deals with relief granted to assesses involved in paying taxes twice that is, paying taxes in India as well as in Foreign Countries or specified territory outside India.

As per section 90, the Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India:

- (a) for granting relief in respect of
 - (i) income on which tax have been paid both under Income Tax Act,1961 and Income-Tax Act prevailed in that country or specified territory or
 - (ii) income-tax chargeable under Income Tax Act, 1961 and under the corresponding law in force in that country or specified territory to promote mutual economic relations, trade and investment, or
- (b) for the avoidance of double taxation of income under Income Tax Act, 1961 and under the corresponding law in force in that country or specified territory.
- (c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under Income Tax Act, 1961 or under the corresponding law in force in that country or specified territory, or investigation of cases of such evasion or avoidance, or
- (d) for recovery of income-tax under Income Tax Act, 1961 and under the corresponding law in force in that country or specified territory

Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India for granting relief of tax, avoidance of double taxation, then, the provisions of Income Tax Act, 1961 shall apply to the assessee to whom such agreement applies, to the extent they are more beneficial to him.

All relief's announced by the Union Government are through Official Gazette. It has been stated in the provision that charge of tax in respect of a foreign company at a higher rate than the rate at which a domestic company is chargeable shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

The benefit of double taxation agreement or tax treaty shall be applicable only when a tax residency certificate is obtained of his resident in any country outside India or specified territory outside India from the Government of that country or specified territory.

ADOPTION BY CENTRAL GOVERNMENT OF AGREEMENT BETWEEN SPECIFIED ASSOCIATIONS FOR DOUBLE TAXATION RELIEF (SECTION 90A)

The Central Government is empowered by section 90A to enter into an agreement with any specified association in the specified territory outside India and the Central Government has been authorized to make such provisions as may be necessary for adopting and implementing such agreement. The provisions may be made:

- (a) for granting relief in respect of
 - (i) income on which tax have been paid both under Income Tax Act, 1961 and Income-Tax Act prevailed in that specified territory or
 - (ii) income-tax chargeable under Income Tax Act, 1961 and under the corresponding law in force in that specified territory to promote mutual economic relations, trade and investment, or
- (b) for the avoidance of double taxation of income under Income Tax Act, 1961 and under the corresponding law in force in that specified territory.
- (c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under Income Tax Act, 1961 or under the corresponding law in force in that specified territory, or investigation of cases of such evasion or avoidance, or
- (d) for recovery of income-tax under Income Tax Act, 1961 and under the corresponding law in force in that specified territory

Where the Central Government has entered into an agreement with the specified association of any specified territory outside India for granting relief of tax, avoidance of double taxation, then, the provisions of Income Tax Act, 1961 shall apply to the assessee to whom such agreement applies, to the extent they are more beneficial to him.

“Specified Association” for this section means any institution, association or body whether incorporated or not, functioning under any law for the time being in force India or the laws of specified territory outside India and which may be notified as such by the Central Government.

“Specified Territory” means any area outside India which may be notified as such by the Central Government for the purpose section 90A. The provision under this section will apply to the assessee to the extent these are beneficial to them. This section provides relief in respect of double taxation in respect to countries with which India has no DTAA.

The benefit of double taxation agreement or tax treaty shall be applicable only when a tax residency certificate is obtained of his resident in any country outside India or specified territory outside India from the Government of that country or specified territory.

COUNTRIES WITH WHICH NO AGREEMENT EXISTS (SECTION 91)

In any previous year, a person resident in India, has paid tax in any country with which India has no bilateral agreement under Section 90 for the relief or avoidance of double taxation in respect of his income which accrued or arose during that previous year under the law in force in that country, by deduction or otherwise,

he shall be entitled to the deduction from the Indian Income Tax payable by him calculated on such doubly taxed income at this Indian Rate of Tax or the rate of the said country whichever is lower or at Indian rate of tax, if both rates are equal.

In case of the assessee stated above earns income from agricultural operation in Pakistan and paid tax thereof can seek relief at rate being lower of the following alternatives namely:

- (i) Tax actually paid in Pakistan
- (ii) Amount computed under Indian Tax Rates.

If any non-resident person is assessed on his share in the income of a registered firm assessed as resident person in India in any previous year and such share includes any income accruing or arising outside India during that previous year (and which is not deemed to accrue or arise in India) in a country with which there is no agreement under Section 90 for the relief or avoidance of double taxation and he proves that he has paid income tax by deduction or otherwise under the law in force in that country in respect of the income so included he shall be entitled:

- to a deduction from the Indian income tax payable by him of a sum calculated on such doubly taxed income so included
- at the Average Indian Income Tax Rate or
- the Average Foreign Tax Rate,

Whichever is lower or at the Indian rate of tax if both the rates are equal.

Indian Tax on doubly taxed income:

$$\frac{\text{Tax on Total Income in India} \times \text{Doubly Taxed Income}}{\text{Total Income in India}}$$

Foreign Tax on doubly taxed income

$$\frac{\text{Tax Paid in Foreign Currency} \times \text{Doubly Taxed Income}}{\text{Total Income in Foreign Country}}$$

Illustration:

Mr. Anuj an individual, resident of India in the previous year receives Professional fees of Rs 1,70,000 on 7th August 2013 and ₹2,55,000 on 15th March 2014 for rendering services in Pakistan on which TDS of ₹30,000 and ₹45,000 have been deducted respectively. He incurred ₹1,60,000 as expenditure for earning this fees. He paid ₹90,000 towards PPF. His Income from other sources is ₹2,60,000. Compute Tax liability & relief under section 91.

Solution:

**Computation of Relief under section 91 of Mr. Anuj
For the Assessment Year 2014-15**

1. Computation of tax liability of Mr. Anuj as per the Income Tax Act, 1961

	₹	₹
Income under the head business & profession:	5,00,000	
Less: Expenditure incurred	<u>1,60,000</u>	3,40,000
Income from other sources		2,60,000
Gross Total income		6,00,000
Less: Deduction u/s 80C: PPF		<u>90,000</u>
Total Income		<u>5,10,000</u>
Tax on ₹5,10,000		32,960
Less: Relief u/s 91		<u>(21,973)</u>
Tax Payable (rounded off)		<u>10,987</u>

2. Computation of relief u/s 91

Doubly Taxed Income = ₹3,40,000

Total Income in India = ₹5,10,000

Tax on total income in India = ₹32,960

Tax paid in foreign country = ₹75,000

Total income assessed in foreign country = ₹ 5,00,000

(a) Tax on such doubly taxed income in India:

$$\frac{32,960 \times 3,40,000}{5,10,000} = ₹ 21,973$$

(b) Tax on such doubly taxed income in foreign country:

$$\frac{75,000 \times 3,40,000}{5,00,000} = ₹ 51,000$$

Relief u/s 91 will be lower of (a) or (b) above i.e. ₹ 21,973/-

NECESSITY FOR DTAA

The need for Double Taxation Avoidance Agreement (DTAA) arises because of rules in two different countries regarding chargeability of income based on receipt and accrual, residential status etc. Double taxation is frequently avoided through DTAAAs entered into by two countries for the avoidance of double taxation on the same income. The DTAA eliminates or mitigates the incidence of double taxation by sharing revenues arising out of international transactions by the two contracting states to the agreement. As there is no clear definition of income and taxability thereof, which is accepted internationally, an income may become liable to tax in two countries. In such a case, the possibilities are as under:

1. The income is taxed only in one country.
2. The income is exempt in both countries.
3. The income is taxed in both countries, but credit for tax paid in one country is given against tax payable in the other country.

If the two countries do not have DTAA then in such a case, the domestic law of the country will apply. In the case of India, the provisions of Section 91 of the Income-Tax Act will apply. The Central Board of Direct Taxes has clarified vide Circular No.333 dated 2nd April, 1982 that in case of a conflict in the provisions of the agreement for Tax Avoidance of double taxation and the Income Tax Act, the provisions contained in the Agreement for Double Tax Avoidance will prevail.

“Economic Liberalization in India” as earlier started from 1991 has covered a wide area touching upon the different fields of international trade, exchange control, monetary and industrial policies, trade and fiscal policies, economic and cultural relations aimed at accelerating the growth in all spheres with a view to bringing about globalization of the India economy. The liberal and broad based economic and commercial relationship between India and various foreign countries in recent years had led to more collaboration and joint ventures at various levels in the public and private sectors to keep pace with the ever changing international advancement in trade, commerce, science and technology. The inflow of multinationals to setup business ventures in India coupled with the funds from Non-residents coming for short-term and long-term investments in India have helped to achieve a sound and stable economy and India today stands recognized internationally. The political situations due to changes in the Governments at the central and state levels

have not adversely affected the growth of international trade and commerce between India and other countries.

The Government of India has entered into numerous tax treaties as well as trade agreements with various foreign countries to provide stability and certainty to the tax laws and commercial relationship between the parties in India and abroad. The large number of judicial pronouncements including advance rulings in the recent years under the tax laws, both direct and indirect, have added to the confidence of Non-residents being inspired with the Indian fiscal and judicial systems. The wealth of judicial decisions from the Supreme Court as well as the High Courts and the tribunals in deciding numerous tax disputes help to remove the uncertainties and ambiguities in the tax system and administration. The tax treaties have helped both the collaborators from abroad and the Indian enterprises in the private and public sectors to know precisely the nature, extent and scope of the tax liability as also the country in which tax is payable.

TAXATION OF INCOME FROM AIR AND SHIPPING TRANSPORT UNDER DTAA

The DTAA is based on four basic models of DTAA and they are – OECD Model Tax Convention (emphasis is on residence principle), UN Model (combination of residence and source principle but the emphasis is on source principle), US Model (it's the Model to be followed for entering into DTAAAs with the U.S. and its peculiar to the US) and the Andean Model (model adopted by member States namely Bolivia, Chile, Ecuador, Columbia, Peru and Venezuela).

Income derived from the operation of Air transport in international traffic by an enterprise of one contracting state will not be taxed in the other contracting state. In respect of an enterprise of one contracting state, income earned in the other contracting state from the operation of ships in international traffic, will be taxed in that contracting state wherein the place of effective management of enterprise is situated. However some DTA agreements contain provisions to tax the income in the other contracting state also, although at reduced rate.

These agreements follow a near uniform pattern in as much as India has guided itself by the UN model of double taxation avoidance agreements. The agreements allocate jurisdiction between the source and residence country. Wherever such jurisdiction is given to both the countries, the agreements prescribe maximum rate of taxation in the source country which is generally lower than the rate of tax under the domestic laws of that country. The double taxation in such cases are avoided by the residence country agreeing to give credit for tax paid in the source country thereby reducing tax payable in the residence country by the amount of tax paid in the source country. These agreements give the right of taxation in respect of the income of the nature of interest, dividend, royalty and fees for technical services to the country of residence. However the source country is also given the right but such taxation in the source country has to be limited to the rates prescribed in the agreement. The rate of taxation is on gross receipts without deduction of expenses.

PERMANENT ESTABLISHMENT (PE)

One of the important terms that occur in all the Double Taxation Avoidance Agreements is the term 'Permanent Establishment' (PE) which has not been defined in the Income Tax Act. However as per the Double Taxation Avoidance Agreements, PE includes, a wide variety of arrangements i.e. a place of management, a branch, an office, a factory, a workshop or a warehouse, a mine, a quarry, an oilfield etc. Imposition of tax on a foreign enterprise is done only if it has a PE in the contracting state. Tax is computed by treating the PE as a distinct and independent enterprise.

Some Salient aspects concerning a PE could be discussed as under:

- PE is defined with reference to place and persons;

- PE could be a fixed place, a construction site, service PE, agency PE branch etc.
- PE denotes non-resident's business preserves. The degree of preserve which could constitute PE has been illustrated by 'inclusions and exclusions'.
- An enterprise is liable to tax on its profits in a foreign country, if it conducts its subsidiary in that country through PE.

Isolated or occasional transactions through some persons or agency do not create liability for tax is the basis of PE. There has to be continuity of activities contributing to the earning of income—something more than mere transaction of purchase and sale or transactions of preparatory or auxiliary nature. Such activities must be value creating activities requiring capital and lesson. 'Permanent' in PE does not mean everlasting.

In order to avoid double taxation it is provided that if a resident of India becomes liable to pay tax either directly or by deduction in the other country in respect of income from any source, he shall be allowed credit against the Indian tax payable in respect of such income in an amount not exceeding the tax borne by him in the other country on that portion of the income which is taxed in the said other country. The same benefit is available to the resident of the other Country, on income taxed in India.

FOREIGN TAX CREDIT

The US Government has opted for foreign credit system being a system involving crediting income tax paid by US entities to the country of the source – as the principal method of accommodation to be used in its international tax relations. The credit is given unilaterally in the IRC and is thus the key factor in the tax calculation relating to foreign income. Tax credit may be direct or indirect.

A direct tax credit is one which is attributable directly on the US tax payers which includes earning from a foreign branch of US Company. Section 901 of the IRC deals with it.

Indirect tax is equal to dividend (including withholding tax) multiplied by foreign tax and divided by earnings net of foreign income taxes.

In no case the credit for taxes paid abroad should exceed the US tax payable on total foreign source income for the same year.

Due to increased globalisation of Indian businesses more and more transactions are being undertaken where the residents need to claim the tax credit of the income-tax paid in other countries. With a view to streamline the process in this regard, some recommendations are given hereinafter:

- (a) The credit for taxes paid overseas should be allowed in the year in which the foreign taxed income is assessable in India;
- (b) The liability towards advance tax should be computed after taking into account the overseas taxes paid.
- (c) Outbound investment from India is on the increase. Some domestic companies have setup subsidiaries in other countries that are generating profits. Normally dividends should flow back to the parent company in India as and when declared. The dividends are, however, flowing to lesser tax jurisdictions where holding companies are being set up.

The income in such jurisdictions accumulates and may be remitted to India at a later date. There is, therefore, a deferment of tax as also a lack of flow back of the funds at an early date. To induce such Indian companies not to structure their affairs in the above manner but to remit the dividend funds to India as also to relieve the economic double taxation on foreign dividend income, a mechanism known as the allowance of underlying tax credit for the stream of dividend income be adopted.

In this scheme, credit is given by the country where the parent company is a resident, not only for the tax withheld at source on the dividend payout by the overseas subsidiary but also in respect of the tax suffered on distributable profits. [Underlying tax = Gross Dividend/Distributable Profits * Actual Tax paid on those profits].

Thus tax in the case of an Indian parent company receiving dividend from more than one tax jurisdiction would be worked out by aggregating the gross dividend, distributable profits and actual taxes suffered on those profits in all such jurisdiction.

This would give an incentive for the flow of funds to the parent Indian company and it would also make them more competitive. Larger availability of funds may generate increased investments by these Indian companies and a source for more taxes for the country.

CASE

Wipro Ltd. v. DCIT – ITA Nos. 895 & 896/Bang/03 and 881 & 882/Bang/03 dated 21st June 2005. In this case the Bangalore Tribunal has held that foreign taxes in respect of income earned abroad will be available as per the provisions of the tax treaty, irrespective of whether income is taxable in India or not provided the income is included in the return of income filed in India. The Tribunal also held that incentive provisions/deductions available should not be brushed aside on a technical consideration. Therefore, even a claim made under Section 80HHE of the Act in the course of assessment proceedings must be entertained. The order of the ITAT deals with various issues including computation of Income under Section 10A/80-IA of the Act.

PASSIVE FOREIGN INVESTMENT COMPANY (PFIC)

A passive foreign investment company is a foreign company with predominantly investment income, or whose assets are primarily intended to generate investment income. The Internal Revenue Service in USA handles the profits of investments in PFICs differently than their domestic counterparts. So US Investors have different tax implications should they hold ownership of a PFIC.

Unlike the controlled foreign corporation provisions, which focus more on tax havens, the PFIC provisions focus on foreign investment structures. Classification as a PFIC occurs when 75% or more of the company's income is passive, or when more than 50% of the company's assets exist in investments earning interest, dividends, and/or capital gains.

The drawback to this tax is that natural resource exploration companies tend to be PFICs because their main assets are the cash they are using to explore with. That cash is earning more interest than the company earns from any other business which brings them under the PFIC definition that was set up to close a tax avoidance loophole.

Tax Code sections 1291 to 1297 of IRC provide the rules for US tax payers who invest in passive foreign investment companies. A foreign corporation is considered a PFIC for these purposes if either of two tests are satisfied: The Income Test or the Asset Test.

Under the Income test, a foreign corporation is considered a PFIC if 75% or more of the foreign corporation's gross income for the taxable year consist of passive income. Passive income includes dividends, interest, royalties, rents, annuities, net gains from certain commodities transactions, net foreign currency gains, income equivalent to interest, payments in lieu of dividends, income from notional contracts, and income from certain personal service contracts. Note that the active business of a licensed bank or insurance business is considered active income; similarly, certain foreign trade income and income allocated to a related person's non-passive income is also excluded.

Under the Asset Test, a foreign corporation is considered a PFIC if 50% of the foreign corporation's assets produce or are held to produce passive income. In applying the Asset Test, the fair market value of the assets is generally used (the FMV method). The general exception is a foreign corporation that is not publicly traded and is a controlled foreign corporation, which must use the adjusted basis of its assets in applying the Asset Test (the Basis Method). A taxpayer may also elect to utilize the basis method, but, once this is done, may not change back to the FMV method without IRS consent.

There are exceptions to these rules for calculation. One is that, Congress has recognized that newly formed corporations frequently hold short term investments that may create a significant percentage of income prior to the business truly commencing. As such, in the first taxable year in which a foreign corporation has gross income, the company will not be considered a PFIC.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation)

1. Discuss the steps for calculating relief under double taxation treaty.
2. Discuss the scope of the provisions the Central Government may make under section 90A(1) of the Income-tax Act, 1961 in respect of an agreement between specified associations.
3. Discuss in brief the provisions regarding double taxation relief.
4. Pawan, aged 66 years and ordinarily resident in India, is a professional. He has earned ₹1,00,000 from services provided outside India. His foreign income was taxed @ 20% in that country where services were rendered. India does not have any tax treaty with that country. Assuming that Indian income of P is ₹3,00,000 What relief of tax under section 91 of the Income-tax Act, 1961 will be allowed to him for the AY 2014-15? Pawan has contributed ₹32,000 towards PPF during the previous year 2013-14.
5. What do you mean by foreign tax credit?
6. Explain briefly the issues involving taxation of PFIC in India.

Answer/Hint

4. Relief u/s 91: ₹ 3,300 and Tax liability: ₹ 8,850.

SUGGESTED READINGS

1. Girish Ahuja & Ravi Gupta : Professional Approach to Direct Taxes-Law and Practice
2. Dr. V K Singhania : Direct Taxes Law and Practices
3. B.B. Lal and N. Vashist : Direct Taxes, Income Tax, Wealth Tax and Tax Planning

Lesson 3

Tax Planning and Tax Management

LESSON OUTLINE

- Concept of Tax Planning
- Tax planning, Tax evasion and Tax avoidance
- Objectives of tax planning
- Importance of tax planning
- Essentials of tax planning
- Types of tax planning
- Some general considerations regarding new business
- Measures of tax planning relating to corporate restructuring
- Tax planning relating to financial management decisions
- Tax planning for Indian collaborators
- Practical Problems
- Lesson Round up
- Self Test questions

LEARNING OBJECTIVES

Tax planning is an exercise undertaken to minimize tax liability through the best use of all available allowances, deductions, exclusions, exemptions etc., to reduce income and/or capital gains while the tax management involves the compliance of law regularly and timely as well as the arrangement of the affairs of the business in such manner that it reduces the tax liability.

This lesson covers tax planning with reference to Corporates and business entities.

At the end of this lesson student will understand:

- What is tax planning, tax avoidance and tax evasion
- What are the tools of tax planning
- How tax planning can be implemented
- Which are the major areas of tax planning
- How to do tax planning with respect to non-resident
- Practical problems covering the tax planning with respect to companies and business entities

Any one may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that Pattern which will best pay the Treasury; there is not even a patriotic duty to increase one's taxes.

—Learned Hand

CONCEPT OF TAX PLANNING

Tax planning can be defined as an arrangement of one's financial and business affairs by taking legitimately in full benefit of all deductions, exemptions, allowances and rebates so that tax liability reduces to minimum.

Example: A deposits ₹45,000 in PPF account so as to reduce his tax payable. This is an example of legitimate tax planning through which tax is reduced.

The Hon'ble Supreme Court in *McDowell & Co. v. CTO* (1985) 154 ITR 148 has observed that "tax planning may be legitimate provided it is within the framework of the law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid payment of tax by resorting to dubious methods." Tax planning should not be done with an intent to defraud the revenue; though all transactions entered into by an assessee could be legally correct, yet on the whole these transactions may be devised to defraud the revenue. All such devices where statute is followed in strict words but actually spirit behind the statute is marred would be termed as colourable devices and they do not form part of tax planning.

Various judicial pronouncements have laid down the principle that substance and form of the transactions shall be seen in totality to determine the net effect of a particular transaction. The Hon'ble Supreme Court in the case of *CIT v. B M Kharwar* (1969) 72 ITR 603 has held that, "The taxing authority is entitled and is indeed bound to determine the true legal relation resulting from a transaction. If the parties have chosen to conceal by a device the legal relation, it is open to the taxing authorities to unravel the device and to determine the true character of relationship. But the legal effect of a transaction can not be displaced by a probing into substance of the transaction."

The form and substance of a transaction is real test of any tax planning device. The form of transaction refers to transaction, as it appears superficially and the real intention behind such transaction may remain concealed. Substance of a transaction refers to lifting the veil of legal documents and ascertaining the true intention of parties behind the transaction.

Recently, a scheme of tax planning, which is being adopted by foreign and domestic investors for quite a number of years for the purposes of investments in businesses in India or abroad, was under the consideration of Supreme Court in the case of *Vodafone International Holdings B.V. v. Union of India* [2012].

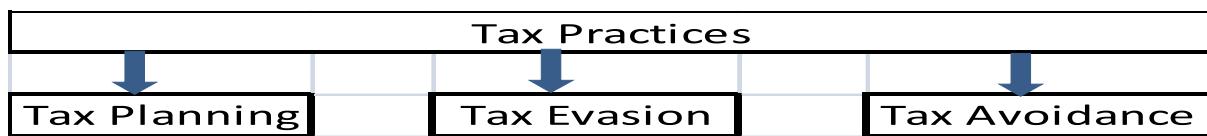
Supreme Court in Vodafone's case accepted that "...if an actual controlling non-resident enterprise makes an indirect transfer through 'abuse of organizational/legal form' and without reasonable 'business purpose' which results in tax avoidance, then the Revenue may disregard the form of the arrangement or the impugned action through use of non-resident holding company, re-characterize the equity transfer according to its economic substance and impose tax on the actual controlling non-resident enterprise. Whether a transaction is used principally as a colourable device for the distribution of earnings, profit and gains, is determined by a review of all the facts and circumstances surrounding the transaction."

However, in the facts of the case Supreme court negated the contentions of the Department and held that "we may reiterate that the 'look at' principle enunciated in Ramsay must look at a document or a transaction in the context to which it properly belongs. It is the task of the Court to ascertain the legal nature of the transaction by looking at the entire transaction and not adopting a dissecting approach.... Every strategic foreign direct investment coming to India, as an investment destination should be seen in a holistic manner. While doing so, Court should keep in mind the following factors: the concept of participation in investment,

the duration of existence of the holding structure, the period of Indian operations, the timing of the exit The onus will be on the Revenue to identify the scheme and its dominant purpose. The corporate business purpose of a transaction is an evidence of the fact that the impugned transaction is not undertaken as a colourable or artificial device."

TAX PLANNING, TAX AVOIDANCE AND TAX EVASION

In India the tax laws are complicated because of various deductions, exemptions, relief and rebates. Therefore, it is logical that taxpayers generally plan their affairs so as to attract the least incidence of tax. However, practice of avoidance is worldwide phenomenon and there is always a continuing battle in this regard between the taxpayer and the tax collector. The perceptions of both are different. The taxpayer spares no efforts in maximising his profits and attracting the least incidence. The tax gatherer, on the other hand, tries to break the plans whose sole objective is to save taxes.



In the context of saving tax, there are three commonly used practices, namely:

(a) Tax Evasion

It refers to a situation where a person tries to reduce his tax liability by deliberately suppressing the income or by inflating the expenditure showing the income lower than the actual income and resorting to various types of deliberate manipulations. An assessee guilty of tax evasion is punishable under the relevant laws.

Tax evasion may involve stating an untrue statement knowingly, submitting misleading documents, suppression of facts, not maintaining proper accounts of income earned (if required under the law) omission of material facts in assessments. An assessee, who dishonestly claims the benefit under the statute by making false statements, would be guilty of tax evasion.

Example: A Industries Ltd. installed an air conditioner costing ₹63,000 at the residence of a director as per terms of his appointment; but treats it as fitted in quality control section in the factory. This is with the objective to treat it as plant for the purpose of computing depreciation. This is an example of tax evasion.

(b) Tax Avoidance

The line of demarcation between tax planning and tax avoidance is very thin and blurred. There is an element of malafide motive involved in tax avoidance.

Any planning which, though done strictly according to legal requirements defeats the basic intention of the Legislature behind the statute could be termed as instance of tax avoidance. It is usually done by adjusting the affairs in such a manner that there is no infringement of taxation laws and by taking full advantage of the loopholes therein so as to attract the least incidence of tax.

Example: A person transferring his assets to another person without adequate consideration to avoid payment of tax on himself.

In the judgement of Supreme Court in McDowell's case (154 ITR 148), tax avoidance has been considered as heinous as tax evasion and a crime against society. Most of the amendments are now aimed at curbing practice of tax avoidance.

The types of cases that come under 'Tax avoidance' are those where the tax payer has apparently circumvented the law, without giving rise to an offence, by the use of a scheme, arrangement or device though of a complex nature, whose main or sole purpose is to defer, reduce or completely avoid the tax payable under the law. Sometimes, the avoidance is accomplished by shifting the liability for tax to other person not at arm's length in whose hands the tax payable is reduced or eliminated.

Example: A foreign company has an Indian subsidiary. Indian subsidiary sells its product to its parent company at a price of ₹100 per unit while the same product is sold to another foreign company at ₹ 200 per unit. In this case, by charging less from its foreign parent company, Indian company is shifting profits outside India to avoid tax liability in India. This would be a case of tax avoidance as transactions are not at arm's length price.

According to G.S.A. Wheat Craft, "tax avoidance is the act of dodging tax without actually breaking the law".

(c) Tax Planning

Tax planning means compliance with the taxation provisions in such a manner that full advantage is taken of all tax exemptions, deductions, concessions, rebates and reliefs permissible under the Income tax Act so that the incidence of tax is the least.

Tax planning can neither be equated to tax evasion nor to tax avoidance with reference to a company, it is the scientific planning of the company's operations in such a way so as to attract minimum liability to tax or postponement or for that matter deferment of the tax liability for the subsequent period by availing various incentives, concessions, allowances, rebates and reliefs provided for in the tax laws. They are meant to be availed of and they have certain clear objectives to achieve.

Example: Doing business in an industrially backward State will entitle an assessee to claim a deduction under section 80-IB. This is an example of tax planning.

DIFFERENCE BETWEEN TAX PLANNING, TAX AVOIDANCE AND TAX EVASION

The line of demarcation between tax planning and tax avoidance is very thin and blurred. There is an element of malafide motive involved in tax avoidance. The type of cases that come under Tax Avoidance are those where the tax payer has apparently circumvented the law, without giving rise to an offence, by the use of a scheme, arrangement or device though of a complex nature, whose main or sole purpose is to defer, reduce or completely avoid the tax payable under the law. Sometimes, the avoidance is accomplished by shifting the liability for tax to other person not at arm's length in whose hands the tax payable is reduced or eliminated. Tax avoidance can be said to be the act of dodging tax without actually breaking the law.

Tax evasion is a method of evading tax liability by dishonest means. Tax evasion can never be construed as tax planning because it amounts to breaking of law whereas tax planning is devised within the legal framework by availing of what the legislature provides. Tax planning ensures not only accrual of tax benefits within the four corners of law but it also ensures that tax obligations are properly discharged so as to avoid penal provisions.

The differences between tax planning, tax avoidance and tax evasion are summarised as under:

Basis	Tax planning	Tax avoidance	Tax evasion
<i>Meaning</i>	It is to avail maximum benefit of deductions, exemptions, rebates etc. for minimizing tax liability.	It refers to reducing the tax liability by finding out loopholes in the law.	It refers to reducing tax liability by dishonest means.

<i>Legality</i>	It is fully within the framework of law and it makes use of the beneficial provisions in law.	It complies with the legal language of the law but not the spirit of the law.	It is clearly violation of law and unethical in nature. It includes an element of deceit.
<i>Example</i>	An enterprise opening a three star hotel to claim deduction under Section 35AD.	An enterprise shifting its income by transfer of its assets to another person.	An enterprise inflating its expenses by showing fake invoices to claim more deductions.
<i>Acceptance</i>	This concept is very well accepted by the Judiciary in India.	This concept can be considered heinous to tax evasion. Government brings amendments to curb such practices and to plug the loopholes.	This is clearly prohibited, as it is fully illegal.
<i>Penalties and Prosecution</i>	It does not result in levy of penalty and prosecution as it is within the language and spirit of law.	It may result in disregarding the transaction done to avoid tax and may/may not result in penalties and prosecution against the person engaged in it.	It results in stringent penalties and prosecution against the person engaged in it.
<i>Time period</i>	It is futuristic in nature i.e. it aims to minimize the tax liability of the future years.	It is also futuristic in nature.	It aims at evading the payment of tax after the liability to tax has arisen.

OBJECTIVES OF TAX PLANNING

The basic objectives of tax planning are:

(a) Reduction of tax liability:

A taxpayer can derive the maximum savings by arranging his affairs in accordance with the requirements of the law. Since every taxpayer wishes to retain a maximum part of his earnings, rather than parting with it and facing the resource crunch, it would be to his benefit to plan his tax affairs properly and avail the deductions and exemptions admissible under the Act. He can succeed in doing so by keeping an awareness of the implications of the various business/other transactions as well as updation of his knowledge about the various concessions for which he is eligible.

Example: A company incurs expenditure on scientific research or provides contribution to National laboratory to claim higher deduction and thereby reducing tax liability.

(b) Minimisation of litigation

Where a proper tax planning is adopted by the taxpayer in conformity with the provisions of the taxation laws, the incidence of litigation is minimised. This saves him from the hardships and inconveniences caused by the unnecessary litigations, which at times even stretch upto the High Court/Supreme Court levels.

Example: Tax planning is not looked upon as bad in the law while tax avoidance by say reducing income of one person by shifting it to another person or tax evasion by showing less income or inflating expenditure attracts litigation, which is neither good for the assessee nor for the Indian judiciary system which is already overburdened with large number of cases.

(c) Productive Investment

Channelisation by a taxpayer of his otherwise taxable income to the various investment schemes too is one of the prime objectives of tax planning as it is aimed to attain twin objectives:

- (i) to harness the resources for socially productive projects, and
- (ii) to relieve the taxpayer not only from the initial brunt of taxation, but also to convert the earnings so made into means of future earnings.

Example: Deductions/Exemptions/Rebates under the Act are primarily to provide incentives for making productive investment e.g. A person can invest in bonds of NHAI or REC to reduce its tax burden on long term capital gain arising on a capital asset by availing exemption under section 54EC.

(d) Healthy growth of economy

The growth of a nation's economy is synonymous with the growth and prosperity of its citizens. In this context, a saving of earnings by legally sanctioned devices fosters the growth of both, because savings by dubious means lead to generation of black money, the evils of which are obvious.

Conversely, tax planning measures are aimed at generating white money having a free flow and generation without reservations for the overall progress of the nation. Tax planning assumes a great significance in this context.

Example: Under the income-tax act, several deductions are provided to boost infrastructure facilities in India i.e. whether it is for making roads or for making hospitals or for making hotels etc. This results in overall growth of the economy by providing incentive to people engaged in these activities.

(e) Economic stability

Proper tax planning results in economic stability by way of:

- (i) availing of avenues for productive investments by the tax payers and
- (ii) harnessing of resources for national projects aimed at general prosperity of the national economy and reaping of benefits even by those not liable to pay tax on their incomes.

Therefore, notwithstanding the legal rulings in cases like McDowell, real and genuine transactions aimed at a valid tax planning cannot be turned down merely on grounds of reduction of the tax burden.

In the context of corporate taxation since the incidence of tax on Indian companies is considered quite high the scope for ploughing back of profits for expansion and modernisation of the existing plant and machinery etc. is considerably narrowed down. Thus the company has to plan its taxation in such a way that will enable it to avail the tax incentives etc. provided by the Government to the maximum.

In this context, it was held in the case of *M.V. Valliapan v. ITO* (1988) 170 ITR 238 (Mad.), by a proper tax planning, a smooth tax flow from the tax payer to the tax administrator, without recriminations, is ensured.

IMPORTANCE OF TAX PLANNING

Tax planning is important for reducing the tax liability. However, there are other factors also, because of which tax planning is considered as very important:

- (i) **Timing is crucial for claiming deductions:** Where an assessee has not claimed all the deductions and relief, before the assessment is completed, he is not allowed to claim them at the time of

appeal. It was held in *CIT v. Gurjargravures Ltd.* (1972) 84 ITR 723 that if there is no tax planning and there are lapses on the part of the assessee, the benefit would be the least.

- (ii) **Tax planning exercise is more reliable:** Tax planning exercise is more reliable since the Companies Act, 1956 and other allied laws narrow down the scope for tax evasion and tax avoidance techniques, driving a taxpayer to a situation where he will be subjected to severe penal consequences.
- (iii) **Incentives by Government to promote activities of public interest:** Presently, companies are supposed to promote those activities and programmes, which are of public interest and good for a civilised society. In order to encourage these, the Government has provided them with incentives in the tax laws. Hence a planner has to be well versed with the law concerning incentives.
- (iv) **Adequate time for tax planning:** With increase in profits, the quantum of corporate tax also increases and it necessitates the devotion of adequate time on tax planning.
- (v) **Enables to bear burden of taxes during inflation:** Tax planning enables a company to bear the burden of both direct and indirect taxation during inflation. It enables companies to make proper expense planning, capital budget planning, sales promotion planning etc.
- (vi) **Capital formation attracts huge deduction:** Capital formation helps in replacing the technologically obsolete and outdated plant and machinery and enables the carrying on of manufacturing operation with a new and more sophisticated system. Any decision of this kind would involve huge capital expenditure which is financed generally by ploughing back the profits, utilisation of reserves and surplus along with the availing of deductions are revenue expenditure incurred for undertaking modernisation, replacement, repairs and renewal of plant and machinery etc. Availability of accumulated profits, reserves and surpluses and claiming such expenses as revenue expenditure are possible through proper implementation of tax planning techniques.
- (vii) **Money saved is money earned:** In these days of credit squeeze and dear money conditions, even a rupee of tax decently saved may be taken as an interest free loan from the Government which perhaps an assessee need not repay.

Thus, any legitimate steps taken by an assessee (being a company) directed towards maximising tax benefits, keeping in view the intention of law, will not only help it but also the society since it promotes the spirit behind the legal provisions. All those companies which practice tax planning may have the satisfaction that they are contributing their best to the nation's broad objectives and goals in a welfare State like ours.

DIVERSION OF INCOME AND APPLICATION OF INCOME

The Supreme Court decision in case of *CIT v. Sitaldas Tirthdas* (1961) 41 ITR 367 is the authority for the proposition that where by an obligation, income is diverted before it reaches the assessee, it is deductible from his income as for all practical purposes it is not his income at all (as it is diversion of income by overriding title) but where the income is required to be applied to discharge an obligation after it reaches the assessee, it is not deductible (as it is called as application of income).

Thus, there is the difference between the diversion of income by an overriding title and application of income as the former is deductible while the latter is not.

Thus, when management of a company is taken over by another person from the existing team in consideration of percentage of future profit to the latter, in computing the business income of the former, such percentage of profits is deductible [*CIT v. Travancore Sugars and Chemicals Ltd.* (1973) 88 ITR 1 (SC)].

The Delhi High Court's ruling in *CIT v. Stellar Investments Ltd.* (1991) 192 ITR 287 to the effect that the Assessing Officer in terms of the power available to him under section 68 of the Act, is not precluded from ascertaining the genuineness of the share capital, must be heeded. There have been occasions when unscrupulous promoters have ploughed back their black money into new companies by subscribing to shares in thousands of fictitious names. If the bluff is called, the unexplained credit in the form of share capital would be treated as income under section 68 of the Act.

ESSENTIALS OF TAX PLANNING

Successful tax planning techniques should have following attributes/requisites:

- (a) **Upto date knowledge of tax laws:** It should be based on upto date knowledge of tax laws. Also, assessee must be aware of judgements of the courts. In addition, one must keep track of the circulars, notifications, clarifications and administrative instructions issued by the CBDT from time to time.
- (b) **Disclosure and furnishing of information to Income-tax department:** The disclosure of all material information and furnishing the same to the income tax department is an absolute prerequisite of tax planning as concealment in any form would attract the penalty clauses – the penalty often ranging from 100% to 300% of tax sought to be evaded.
- (c) **Planning to be within the framework of law:** Whatever is planned should not only satisfy the requirements of law by complying with legal provisions as stated and meeting the tax obligations but also should be within the framework of law. It means that sham transactions or make-believe transactions or colourable devices, which are entered into just with a view to circumvent the legal provisions, must be avoided.

A genuine tax planning device, aimed at carrying out the rules of law and courts' decisions and to overcome heavy burden of taxation, is fully valid.

- (d) **Capability to achieve desired objectives and amenable to changes:** A planning model must be capable of attainment of the desired objectives of a business and be amenable to its possible future changes. Therefore, all the important areas of corporate planning, whether related to strategic planning, project planning or operational planning involving tax considerations for long term or short term management objectives and policies should be strictly scrutinised in relative situations. Foresight is the essence of a business. Tax planning is one of its important attributes.

TYPES OF TAX PLANNING

The tax planning exercise ranges from devising a model for specific transaction as well as for systematic corporate planning. These are:

(a) Short range and long range tax planning

Short range planning refers to year to year planning to achieve some specific or limited objective. For example, an individual assessee whose income is likely to register unusual growth in particular year as compared to the preceding year, may plan to subscribe to the PPF/NSC's within the prescribed limits in order to enjoy substantive tax relief. By investing in such a way, he is not making permanent commitment but is substantially saving in the tax. It is one of the examples of short range planning.

Long range planning involves entering into activities, which may not pay off immediately. For example, when an assessee transfers his equity shares to his minor son, he knows that the income from the shares will be clubbed with his own income. But clubbing would also cease after minor attains majority.

(b) Permissive tax planning

It is tax planning under the express provisions of tax laws. Tax laws of our country offer many exemptions and incentives.

(c) Purposive tax planning

It is based on the measures which circumvent the law. The permissive tax planning has the express sanction of the Statute while the purposive tax planning does not carry such sanction. For example, under Section 60 to 65 of the Act, the income of the other persons is clubbed in the income of the assessee. If the assessee is in a position to plan in such a way that these provisions do not get attracted, such a plan would work in favour of the tax payer because it would increase his disposable resources. Such a tax plan would be termed as 'Purposive tax planning'.

TAX MANAGEMENT

Tax Management involves the compliance of law regularly and timely as well as the arrangement of the affairs of the business in such manner that it reduces the tax liability. Functions under tax management includes filing of return, payment of tax on time, appear before the Appellate authority etc.

Tax management emphasizes on compliance of legal formalities for minimization of taxes while tax planning emphasis on minimization of tax burden.

AREAS OF TAX PLANNING IN THE CONTEXT OF THE INCOME-TAX ACT, 1961

Some of the important areas where planning can be attempted in an organised manner are as under:

1. At the time of setting up of new business entity:

- (a) Form of organisation/ownership pattern;
- (b) Locational aspects;
- (c) Nature of business

2. For the business entities already in existence:

- (a) Tax planning in respect of corporate restructuring;
- (b) Tax planning in respect of financial management;
- (c) Tax planning in respect of employees remuneration;
- (d) Tax planning in respect of specific managerial decisions;
- (e) Tax planning in respect of Foreign collaborations and Joint Venture Agreements;
- (e) Tax planning in the light of various Double Taxation Avoidance Agreements (DTAA)

FORM OF THE ORGANISATION

The selection of particular form of organisation depends not only on the magnitude of financial requirements and owner's liability, but also on the tax considerations. Normally, depending upon the level of operation, expected profitability, need for external financing and expected requirements of technical expertise, a suitable form can be chosen.

In view of the continuity of business, the benefits arising out of limited liability, organised accounting and the overall long-term tax benefits flowing to the company form of organisation, the corporate enterprises may be

regarded as an effective instrument of tax planning. The company being a separate legal entity confers certain valuable benefits in the matter of tax planning to its shareholders and the persons connected with the management of the company.

(A) COMPANY FORM OF THE ORGANISATION

The important tax privileges and advantages to a company over the other forms can be summarised as under:

- (a) **Deduction of Remuneration for managing persons:** Remuneration is allowed for the persons who are managing the affairs of the company and also owning its shares.
- (b) **Clubbing provisions do not apply:** The provisions relating to clubbing of income u/s 64 of the Act do not apply even if the business is carried on by family members through a company, which ultimately leads to reduction in liability to tax on the part of the individual members.
- (c) **Dividend from Indian company is exempt:** Dividend received by the shareholders from any Indian company as referred to in Section 115-O is exempt under Section 10(34) of the Act.
- (d) **Deductions available to companies results in minimization of incidence of tax substantially:** Companies are subjected to flat rate of tax, regardless of quantum of their income. The tax rate on domestic companies is 30% plus applicable surcharge and cess. This, however, may not seem to be an advantage in view of low slab rates applicable to sole proprietorships, but when we look at the total incidence of tax after taking into account the various deductions allowed to companies and the scheme of perquisites, the real owners of companies to stand to benefit.
- (e) **Certain benefits to company only:** There are certain special tax concessions, allowances and deductions given under the Act available only to the company form of business enterprises such as deductions allowed under Section 33AC, Section 36(a)(ix) and 35D of the Act.
- (f) **Shares in a company an attractive investment:** The shares in companies are treated as long term capital assets qualifying for considerable leniency in taxation even if they are held by the assessee for a small time as 12 months. This has made investment in the shares of companies all the more attractive. This helps the companies to generate the funds required for their development as well as furtherance of their objects.
- (g) **No wealth tax on shares:** There is no wealth tax on shares of a company.

Tax liability is an important consideration guiding the choice of a legal form of business organisation. In some circumstances, however this consideration is of no significance. For example large business is generally compelled to organise itself in the form of a company as this form of organisation makes it possible to raise large amounts of capital required. Similarly retail business of small size can only be economically operated as proprietorship or partnership firm. When there is freedom of choice, taxation becomes an important consideration.

In most cases, company form of organisation is to be preferred from long term point of view. There are certain other dimensions in this context, one of which is the preference for a widely held company as against a closely held company so much that we would suggest conversion of an existing closely held company into a widely held company as it would be enjoy the following tax benefits over a closely held company:

- (a) **No limitations with regard to set off and carry forward of losses:** Widely held companies do not find limitations and restrictions in the matter of set off and carry forward of losses whereas closely held companies have certain limitations or restrictions in this respect under Section 79 of the Act.

In the case of companies in which the public are not substantially interested, losses will not be carried forward and set off unless the shares of the company carrying atleast 51% of the voting power were beneficially held by the same person(s) both on the last day of the previous year in which loss occurred and on the last day of the previous year in which brought forward loss is sought to be set off.

However, if a change in voting power as aforesaid takes place consequent upon the death of a shareholder or on account of transfer of shares by way of gift to any relative of the shareholder making such gift, then the aforesaid disability does not get attracted.

This disability is also not attracted where change in the shareholding of an Indian company which is a subsidiary of a foreign company, takes place as a result of amalgamation or demerger of a foreign company subject to the condition that fifty one percent shareholders of the amalgamating or demerged foreign company continue to be the shareholders of the amalgamated or the resulting foreign company.

The provisions of Section 79 of the Act are applicable in the case of carry forward and set off of losses only. As carry forward of unabsorbed depreciation allowance, investment allowance, development rebates and development allowance stands on an altogether different footings; their carry forward and set off is not governed by Section 79 as per Madras High Court in *CIT v. Concord Industries Ltd.* (1979) 119 ITR 458.

- (b) **Provisions of deemed dividend u/s 2(22)(e) applicable to closely held company only:** The provisions of deemed dividend in respect of advances or loans to shareholders, or any payment on behalf of shareholders or any payment for the individual benefit of a shareholder are applicable to a closely held companies under Section 2(22)(e) of the Act.
- (c) **Conversion from closely held company to widely held company would not result in transfer of ownership and no tax liability:** The conversion would not be treated as transfer of ownership of the business and hence, there shall be no liability for capital gains tax or income tax in the hands of the closely held company or the new widely held company, due to conversion.

(B) REGISTRATION OF CHARITABLE INSTITUTIONS AS COMPANIES

Associations having charitable object viz., promotion of commerce, art, science, religion, charity or any other useful object by nature, can be registered as companies under Section 25 of the Companies Act, 1956 and avail the benefits of a company form of organisation from the point of view of the Companies Act, as well as various tax concessions available to widely held companies under the Act and also claim exemption from Income tax under section 11 of the Act subject to the conditions specified in Section 13 thereof.

(C) PARTNERSHIP FIRM OR LIMITED LIABILITY PARTNERSHIP

A partnership form of organization is easy to establish. The only procedure for the formation of partnership is to draw up a partnership deed. This form of organization is suitable due to the following factors:

- (a) **Quick decision making:** The decision making on important business matter is quick as compared to a company form of organization because partners meet frequently together.
- (b) **Less risky:** The chance of getting involved in risky activities is very less because every important decision is made with the concurrence of all the partners.
- (c) **Additional resources can be arranged easily:** As compared to sole proprietorship, the problem of raising additional resources is much less. Whenever the business expands and it is necessary to raise finance, it will be easy to raise it by admitting a new partner or raising it by way of borrowing

because of number of partners and their joint and several liability to pay the debts of the firm, the lenders will be more interested in lending.

- (d) **Remuneration and interest to partners allowed:** The firm can pay interest on capital and loan to partners at the maximum rate of 12% p.a. Further, it can also give remuneration to its working partners subject to the limits mentioned in Section 40(b). Firm's profits are taxable after allowing interest and remuneration to working partners.
- (e) **Suitable in cases where firm's profits are not large:** This form of organization is suitable from income-tax point of view in such cases where the amount of profit is not large and the partners of the firm do not have any other additional income except by way of remuneration and interest from the partnership firm. In such a case the profit of the firm shall be lower and the individual partners can also avail of the maximum ceiling of income exempt under the Act.
- (f) **Share of partners' in firm's profit is exempt:** The share in the profit of the partnership firm is exempt from tax under section 10(2A) of the Act.
- (g) **Risk of losses is divided:** The risk as to losses and liability incurred is divided amongst the partners.
- (h) **No tedious procedure for change of business:** In the case of a company form of organization, the change of business requires a long procedure while there is no tedious procedure in the partnership form of organization. The business can be changed only with the consent of partners.

However, this form of organization is not suitable due to the following reasons:

- (i) **Limited risk taking capacity of partner:** Every decision relating to important business matters is made with the consultation of other partners, which restricts the risk taking activities which may yield much higher profits.
- (ii) **Financing in case of expanding business:** When business gets expanded to a large scale, then it will be suitable to adopt a company form of organization because partnership can be formed up to maximum 20 partners.
- (iii) **Partners' unlimited liability:** Partner's liability is unlimited and recovery can be done from his personal assets also. It may also happen that one partner becomes liable for the acts of another. Therefore, a partner is liable for the wrongs of another partner if it is done within the legal limits.
- (iv) **Limitation on deduction of remuneration and interest:** Deduction of remuneration to partners and interest on partners' capital is allowed subject to limits prescribed under section 40(b). Also, such amount allowed to partnership firm is taxable in the hands of employees.
- (v) **No deduction of remuneration and interest for non-compliance with section 184:** Where the partnership firm does not comply with the requirements of section 184 of the Income-tax Act, although the firm shall be assessed as firm, it shall not be allowed any deduction on account of interest and remuneration to partners.
- (vi) **Sudden closure:** A partnership may come to a sudden closure of business on account of death, lunacy or insolvency. In the case of a business running efficiently and profitably, such happening will cause a great loss. Also, dissolution will attract section 45(4) which imposes tax liability in respect of capital gain arising on transfer of capital asset from the firm to partners.

Limited Liability partnership:

Entrepreneurs now have an alternative and innovative form of business organization i.e. Limited liability partnership (LLP) which combines the benefits of company and general partnership form of business organizations. LLP has separate legal entity, perpetual succession and limited liability of partners.

From income-tax point of view, LLP is treated as general partnership firm and therefore, its profits will be taxed in the hands of the LLP and not in the hands of its partners.

(D) SOLE PROPRIETORSHIP

The most common form of ownership found in the business world is sole proprietorship. In this form of organization, the proprietor is the only owner of the business assessed and he is solely responsible for the affairs of the business. This form of organisation is suitable due to the following factors:

- (a) **Easy to establish:** A sole proprietorship is easy to establish because of little interference of government regulations.
- (b) **Less cost:** The cost of adopting this form of organization is small because of there being no legal requirement.
- (c) **Profits to owner only:** All the profits of the business go in the hands of proprietor himself.
- (d) **Basic exemption limit and least tax liability:** In case of persons carrying on small scale and having small income from other sources, this form of organization would be suitable because the proprietor can avail basic exemption limit as under:

For Assessment Year 2014-15	₹
i. In case of individuals in India below 60 years of age	2,00,000
ii. In case of individuals resident in India who is of the age of 60 years but below the age of 80 years at any time during the previous year	2,50,000
iii. In case individual who is of the age of 80 years or above	5,00,000

The tax liability of the individual will be minimum as the individual is subject to income-tax at slab rate.

- (a) **More deductions available under Chapter VIA:** Besides the deductions allowed to all assessee under Chapter VIA, a sole proprietor is entitled to get certain deductions under the following sections:
 - (i) **Section 80C:** It relates to contributions to provident fund, life insurance premium, subscription to certain equity shares or debentures, etc.
 - (ii) **Section 80CCC:** It relates to contribution to certain pension funds.
 - (iii) **Section 80CCD:** It relates to contribution to notified pension scheme of the Central Government.
 - (iv) **Section 80D:** It relates to medical insurance premium.
 - (v) **Section 80DD:** It relates to maintenance of a dependant who is a person with disability.
 - (vi) **Section 80DDB:** It relates to expenditure on medical treatment etc.
 - (vii) **Section 80E:** It relates to interest on loan taken for higher education.
 - (viii) **Section 80GG:** It relates to rent paid.
 - (ix) **Section 80QQB:** It relates to royalty income etc. of authors of certain books other than text books.
 - (x) **Section 80RRB:** It relates to royalty on patents.
 - (xi) **Section 80U:** It relates to persons with disability.

However, this form of organization is not suitable due to:

- (a) **Unlimited liability:** The liability of the proprietor is unlimited and it can extend even to his personal assets.
- (b) **No deduction for remuneration and interest on capital:** The proprietor does not get deduction on account of remuneration payable to him for rendering services. It is felt that it is the capital contributed and risk taken by the proprietor for which he is rewarded in profits and that he must be given remuneration for the services rendered by him which should be allowed as deductible expenditure. But this is not so in income-tax law.
- (c) **Limited opportunities to finance:** This form of organization does not provide opportunities to finance the expanding business activities unlike partnership or LLP or company which can finance expanding business by including more partners/members.

(E) HINDU UNDIVIDED FAMILY (HUF)

(a) Slab Rate: A joint HUF pays tax on its total income at prescribed rates on the basis of slab system. A HUF will also get a basic exemption of ₹2,00,000 for AY 2014-15. The tax rates on HUF are same as applicable to Individual.

(b) Remuneration to Karta and members allowed: The family can pay reasonable remuneration to the Karta and other family members for their services to the business and it is allowable as a deduction in computing the business income.

The members of the family, who have received the remuneration from the family will include it in their income under the head Salaries.

Interest on capital contributed by the family for the business is not deductible in computing the business income.

(c) Deductions: Besides, the deduction which are allowed to all assessee, it is allowed certain deductions under section 80C, 80D, 80DD, 80DDB and 80GG like individuals.

The demerits of HUF, however, are similar to that of Individuals.

LOCATIONAL ASPECTS

Tax planning is relevant from location point of view. There are certain locations which are given special tax treatment. Some of these are as under:

- (a) **Newly established undertaking in free trade zones etc.:** Full exemption under Section 10A is available in the case of a newly established Industrial undertaking in free trade zones, etc. (not allowed w.e.f. AY 2012-13).
- (b) **Newly established units in SEZ:** Full exemption under Section 10AA for initial five years, 50% for subsequent five years and further deduction of 50% for a further period of five years in case of a newly established units in SEZ on or after 1.4.2005.
- (c) **Newly established 100% EOU:** Full exemption under Section 10B for 10 years in the case of a newly established 100% export-oriented undertaking. (Not allowed w.e.f. AY 2012-13).
- (d) **Developer of SEZ:** Deduction under Section 80-IAB in respect of profits and gains by an undertaking or an enterprise engaged in the development of SEZ.
- (e) **Industrial undertaking in Industrially backward state or district:** Deduction under Section 80-IB

is allowed in the case of a newly set up industrial undertaking in an industrially backward State or district.

- (f) **Industrial undertaking in certain special category States:** Deduction under Section 80-IC is available in case of newly set up industrial undertaking or substantial expansion of an existing undertaking in certain special category States.
- (g) **Hotels and convention centres in specified area:** Deduction under Section 80-ID is allowed in respect of profits and gains from business of hotels and convention centres in specified area or a hotel at world heritage sites.
- (h) **North-eastern States:** Deduction under Section 80-IE is allowed in respect of certain undertakings in North-Eastern States.

NATURE OF BUSINESS

Tax planning is also relevant while deciding upon the nature of business. There are certain businesses which are granted special tax treatment. Some of these are as follows:

- (a) Newly established units in Free Trade Zones [Section 10A – Not available w.e.f. AY 2012-13], SEZ [Section 10AA] and EOU [Section 10B- Not available w.e.f. AY 2012-13].
- (b) Tea Development Account, Coffee Development Account and Rubber Development Account [Section 33AB];
- (c) Site Restoration fund [Section 33ABA];
- (d) Specified business eligible for deduction of Capital Expenditure [Section 35AD];
- (e) Amortisation of certain preliminary expenses [Section 35D];
- (f) Expenditure on prospecting for certain minerals [Section 35E];
- (g) Special reserve created by a financial corporation under Section 36(1)(viii);
- (h) Special provisions for deduction in the case of business for prospecting for mineral oil [Section 42 and 44BB];
- (i) Special provisions for computing profits and gains of business on presumptive basis [Section 44AD];
- (j) Special provisions in the case of business of plying, hiring or leasing goods carriages [Section 44AE];
- (k) Special provisions in the case of shipping business in the case of non-residents [Section 44B];
- (l) Special provisions in the case of business of operation of aircraft [Section 44BBA];
- (m) Special provisions in the case of certain turnkey power projects [Section 44BBB];
- (n) Special provisions in the case of royalty income of foreign companies [Section 44D];
- (o) Special provisions in case of royalty income of non-residents [Section 44DA];
- (p) Certain income of offshore banking units and International financial service centre [Section 80-LA];
- (q) Profits and gains of industrial undertakings or enterprises engaged in Infrastructure development etc. [Section 80-IA].
- (r) Profits and gains of an undertaking or an enterprise engaged in development of SEZ [Section 80-IAB];

- (s) Profits and gains from certain industrial undertaking other than infrastructure development undertaking [Section 80-IB];
- (t) Special provisions in respect of certain undertakings or enterprises in certain category States [Section 80-IC];
- (u) Deduction in respect of profits and gains from business of hotels and convention centres in specified area or a hotel at world heritage site [Section 80-ID].
- (v) Special provisions in respect of certain undertakings in North-Eastern States. [Section 80-IE];
- (w) Profits and gains from the business of collecting and processing of bio-degradable waste [Section 80JJA];
- (x) Employment of new workmen [Section 80JJAA];
- (y) Special tax rates under Section 115A, 115AB, 115AC, 115AD, 115B, 115BB, 115BA and 115D.

SOME GENERAL CONSIDERATIONS REGARDING NEW BUSINESS

- (a) **Separate Accounts:** It is advisable, though not a statutory obligation, to keep the accounts of the new business separate. This obviates the necessity of making any estimates, complicating the state of affairs of the new business.

In this connection, reference may be made to *CIT v. Dunlop Rubber Co. (I) Ltd.* (107 ITR 182):

In this case, the existing company established a new factory and no separate accounts were maintained by the new unit. But, as a matter of fact, this was not essential for claiming the benefit. In this case, the assessee claimed the benefit on the proportion of turnover between the new unit and old unit. Was the method adopted correct? The duty of Revenue Department was to determine the exemption allowed by law.

It was held:

“It was the duty of the I.T.O. under Sections 143 to 145 of the Act, to determine the total income of the assessee and determine the tax payable, even if the income could not be derived from the books of the assessee. So, Income-tax officer cannot deny the relief. Difficulty in computing the relief cannot be a ground for rejecting the claim. A rule of apportionment consistent with commercial accounting must be evolved in computing the income. If the assessee already followed certain system, which is in vogue in general, from a commercial accounting angle, and if the Income-tax Officer disputes such system, he should correct it and cannot reject it as whole-sum. In this case it was held that the Income-tax Officer could not refuse the claim for exemption.”

Supreme Court in *Textile Machinery Corporation Ltd. v. CIT* (108 ITR 195) inter-alia, held that the fact that there was common management or the fact that separate accounts had not been maintained, would not lead to the conclusion that they were not separate undertakings. Even if separate account is not maintained, the investment in each of the units can be reasonably determined with the material which the assessee may make available to the department. The test is whether it is a new and identifiable undertaking separate and distinct from the existing business. It is sufficient if the new undertaking is an integrated unit by itself wherein articles are produced and a minimum of 10 persons are employed.

In *Mahindra Sintered Products Ltd.* (177 ITR 111), the Bombay High Court held that it was not necessary that separate accounts had to be maintained but separate accounts kept in the ledger are sufficient to claim deduction under Section 80J.

Further, it was held by the Bombay High Court in *CIT v. Mazaggon Dock Ltd.* (191 ITR 461) that the maintenance of separate account is not a condition precedent for claiming special deduction under Section 80J.

Although Section 80J is omitted w.e.f. 1.4.1989, the ratio is applicable on other deduction available.

- (b) **Avoid interconnection between new business and any other activity:** Avoid interconnection of service or departmental centralisation or pooling of resources of the new business and any other activity of the assessee.
- (c) **Avoid transfer of goods between existing activities and new business:** Avoid transfer of goods between the new business and the assessee's other activities and encourage only cash flows out of sale proceeds towards investment or capital purpose.
- (d) **Separate agreements etc. for new business:** It is better for the new business to have separate floor area, separate licenses and agreements, if it is not related to the assessee at all. Even separate profit computation should be encouraged. However, the total income should be computed as per the scheme of the Act. [*CIT v. Kashmir Fruit and Chemical Industries* (98 ITR 311) J & K High Court]
- (e) **Absorb deficiency in capital intensive industries:** In case of capital intensive industries having long gestation periods; generally profit earning would be delayed. This is true even in the case of complicated and time consuming manufacturing processes. In such circumstances, it is quite likely that only deficiency would be absorbed.
- (f) **Each industrial unit to be treated separately for tax holiday:** Each industrial unit (for example, weaving and spinning units in case of textile business) of an industrial organisation has to be considered for computing the tax holiday benefit.
- (g) **Deduction for expenditure on scientific research:** Any capital or revenue expenditure incurred towards scientific research u/s 35 will be treated as mentioned therein.

SETTING UP AND COMMENCEMENT OF BUSINESS VIS-À-VIS TAX PLANNING

Setting up a business within the scope of the Act is a particular point to be considered for the purpose of tax planning strategy. It is different from the commencement of business. The company may be incurring certain expenditure of revenue nature during the intervening period after setting up and before the commencement of business (production). It is provided in the tax laws that the general expenses prior to the date of setting up are inadmissible but those incurred from the date of setting up and before the commencement of the business may be allowed as deduction for tax purposes provided they are of revenue nature and are incurred wholly and exclusively for the purpose of business.

From the decisions of the Bombay High Court in *Western India Vegetable Products Ltd. v. CIT* (1954) 26 ITR 151 (BOM) and the Supreme Court in *CIT v. Ramaraju Surgical Cotton Mills Ltd.* (1967) 63 ITR 478(SC) and *Travancore Cochin Chemical Pvt. Ltd. v. CIT* (65 ITR 651), it has been well settled that a business is set up as soon as it is ready to commence production and it is not necessary that the actual production should be so commenced. It is also observed that the business commences with the start of first activity in point of time and which must necessarily precede other activity.

In the case of *CIT v. Saurashtra Cement and Chemical industries Ltd.* (91 ITR 170) the Gujarat High Court had held that 'Business' connoted a continuous course of activities. All the activities which go to make up the business need not be started simultaneously in order that the business may commence. The business would commence when the activity which is first in point of time and which must necessarily precede all other activity is started.

Reliance on the above case was placed by the Allahabad High Court in the case of *Mod Industries Ltd. v. CIT* (1977) 110 ITR 855, while deciding the question of allowance of business expenditure, it was held in this case that the foreign tour expenses of the chairman for setting up of two new factories were not allowable as business expenditure under Section 37 and were of a capital nature.

The decision of Sarabhai Management Corporation Ltd. (supra) was also relied upon in the case of *Hotel Alankar v. CIT* (1982) 133 ITR 866 and *CIT v. O.P. Khanna and Sons* (1983) 140 ITR 558.

The Andhra Pradesh High Court laid down the following principles to determine whether a business has commenced or not in *CIT v. Sponge Iron India Ltd.* (1993, 201 ITR 770): Whether a business has commenced or not is a question of fact.

- (a) There is a distinction between the setting up of business and the commencement of business.
- (b) Where the business consists of a continuous course of activities, for commencement of business all the activities which go to make up the business need not be started simultaneously. As soon as an activity which has the essential activity in the course of carrying on the business is started, the business must be said to have commenced.

In this case, it was held, on facts, that since the business had not commenced, the interest income could not be treated as business income. It was also held that the assessee was not entitled to the deduction of the administrative expenses and exploration and mining expenses from out of its interest income.

Income pending setting up of business:

It is possible that pending setting up of business, the funds raised by a company may be invested temporarily so that they do not remain idle. Income from such investments are taxable under Income from Other Sources. Expenses pending setting up of business like salary to staff, office expenses etc. cannot be deducted from such investment income [*Traco Cable Co. Ltd. v. CIT* (1969) 72 ITR 503 (Ker.)].

Companies in such a scenario are in unenviable position. On the one hand, they are incurring expenses which go a begging and on the other, they have income from investments which are taxed.

The Madras High Court in *CIT v. Seshasayee Paper & Boards Ltd.* (1985) 156 ITR 542 (Mad.) held that set off under Section 72 of the Act is also not possible because the expenses on business if they are not allowable as a deduction, cannot assume the form of loss either so as to qualify for set off against income from investments. Companies may therefore expedite setting up of business so that the business loss may be set off against such income from other sources.

It may be noted that the view expounded by the Madras High Court in Seshasayee (supra) has been endorsed by the Supreme Court in *Tuticorn Alkale Chemicals & Fertilisers Ltd. v. CIT* (1997) 27 CLA 41.

In the judgement of *CIT v. Bokaro Steel Ltd.* (33 CLA (Sur.) 18), the Supreme Court has pointed out that where it is possible to establish a link between investment income pending commencement of business with the cost of project, the same can be reduced from the cost of assets it has in fact gone to subsidise.

MEASURES OF TAX PLANNING IN RELATION TO SETTING UP AND COMMENCEMENT

- (a) **Achievement of setting up at the earliest:** A company which has planned the Installation programme should see that the setting up of the business is achieved at the earliest, though the actual commencement of business may come later depending upon the other relevant considerations weighing with the company, i.e. postponing the production for some period if the comparative position of incomes and losses permit, enabling the company to avail the benefit of tax

holiday, investment allowance, carry forward of unabsorbed losses and depreciation for a longer period.

- (b) **Expenditure revenue in nature and incurred exclusively for business:** Expenses after setting up of the business must be of revenue nature and they should be incurred wholly and exclusively for business purpose for being admissible for deduction. For the purpose of the business is different from "for the purpose of earning profits" as it means the expenditure should be for the carrying on of the business and the assessee should incur it in his capacity as a person carrying on the business. [*CIT v. Muir Sugar Mills Co. Ltd.* (1980) 123 ITR 534 (Allahabad HC)].

Such expenditure may constitute a part of the preliminary expenditure and may be eligible for amortisation over a period of five years u/s 35D of the Act.

- (c) **Certain tax holidays operative from commencement of business:** The term commencement of business is also important in the case of a newly established industrial undertaking. The tax holiday under the provisions of Section 80-IA and 80-IB of the Act also becomes operative from the point of time production is commenced and continues upto the prescribed period.
- (d) **Preliminary expenditure allowable from year of commencement:** Under the provisions of Section 35 of the Act, any expenditure whether capital or revenue, incurred on scientific research, during the three accounting years immediately preceding the year of commencement of business is allowed as deduction in the year of commencement of business. The company may proceed to assess the past period of three years or so and compare the amount of expenditure incurred or expected to be incurred in the forthcoming period and thereby can avail of the maximum benefit by adjusting the time of commencement of business accordingly.

TAX PLANNING RELATING TO CORPORATE RESTRUCTURING

The following suggestions could be useful for tax planning in respect of amalgamation, merger, demerger etc.:

- Planning for carry forward and set off of unabsorbed losses and unabsorbed depreciation:** Since the unabsorbed losses and unabsorbed depreciation cannot be allowed to be carried forward and set off in the hands of the amalgamated company, except in the cases prescribed under Section 72A of the Act, it is proposed:
 - that the scheme of the amalgamation can be put off till such time the full benefit of set off is availed of by the amalgamating company; and
 - that the loss carrying company should absorb or take over the business of profit making company. In other words, the profit making company should merge itself with the loss incurring company. This would help in carrying to carry forward the benefits of all unabsorbed losses and depreciation to be set off against the profits derived from the business of the profit making company.
- Allowability of bad debts in amalgamation scenario:** To save from disallowance of the debts of the amalgamating company which subsequently become bad in the hands of the amalgamated company, the amalgamated company should plan to make suitable provision for the expected losses on account of bad debts at the time of fixing the consideration while taking over the business of the amalgamated company.

However, in view of the Court judgement of *CIT v. T. Veerabhadra Rao* (1985) 22 Taxman 45, the bad debts are not allowed to an assessee by way of personal relief but to a business. So, it is possible for the amalgamated company to claim bad debts even in respect of debts taken over from the amalgamating company.

3. **Amalgamation of a unlisted company with a listed company:** A company whose shares are not quoted on a recognised stock exchange may avail the benefit of amalgamation by amalgamating itself with another company whose shares are quoted on a recognised stock exchange. This would help its shareholders to take the advantage of the quoted price of their shares in the stock exchange while determining their liability for wealth tax purposes.
4. **Amalgamation of a company holding immovable properties with an Industrial company:** A company holding investments in immovable properties may avail the benefit of non applicability of the provisions of the Urban Land Ceiling Act by amalgamating itself with an Industrial company.
5. **Amalgamation of loss incurring company and profit making company to reduce tax incidence:** A loss incurring company and a profit making company may merge in order to reduce the overall incidence of liabilities to tax under the Income-tax Act, 1961.
6. **Reverse merger:** In case the conditions provided under Section 2(1B) and 72A of the Act are not satisfied, it may be suggested that the profit making company should merge itself with the loss making company, so that the loss making company does not lose its existence and also enjoys all other benefits.
7. **Reduction of dissenting shareholders to complete amalgamation:** Under Section 2(1B) of the Act, it is provided that for availing the benefits of amalgamation, atleast 75% of the shareholders of the amalgamating company should become shareholders of the amalgamated company. In case more than 25% of the shareholders are not willing to become shareholders of the amalgamated company, it is proposed that the amalgamating company may persuade the other shareholders who may be willing, to purchase the shares in the amalgamated company to acquire the shares of the remaining shareholders so that the percentage of dissenting shareholders does not exceed 25%. Alternatively, the amalgamated company prior to amalgamation may purchase shares from such dissenting shareholders so as to make such dissenting shareholders to go below the specified percentage of 25%.

CONCEPT OF REVERSE MERGER

There is a recent trend of going in for reverse merger. It means that the profit making company merges into the sick company thereby becoming eligible to carry forward of losses etc. without the aid of Section 72A of the Act. The profit making or healthy company extinct and loose its name and the surviving sick company retains its name. It is actually device to bypass merger under section 72A of the Act and is being increasingly popular now a days.

Invariably soon after the merger or after a year or so, the name of the company is changed to accord with that of the profit making amalgamating company. In this way, two birds are killed with one stone because:

- (a) Losses are carried forward, which would otherwise have not been possible;
- (b) Goodwill, which consists, in the name of the profit making amalgamating company, is also retained.

The same route was followed among others, by Kirloskar Pneumatics Ltd. where the company merged with Kirloskar Tractors Ltd., a sick unit and initially lost its name but after one year it changed its name as was prior to merger. However, it remains to be seen whether the Parliament/Judiciary views this kind of strategy as an exercise resulting in tax-avoidance or not? But, right now, this is not required in view of changes done in Section 2(1B) and 72A of the Act.

TAX PLANNING RELATING TO FINANCIAL MANAGEMENT DECISIONS

Following points need to be considered while planning Financial management decisions:

- (a) **Expenses on issue of debentures/deposits should be after setting up of business:** When a company raises long term loans from financial institutions or by way of public issue of debentures or inviting deposits from the public, it should plan that the expenses incurred on such issues of debentures or expenses towards stamp duty, registration fees and lawyer's fees should be incurred only after the date of the setting up of the business.
- (b) **Interest paid for acquisition of fixed assets to be capitalized:** The interest paid before the commencement of production but after setting up of the business on loans taken by the company for the acquisitions of its plant and machinery and other assets, forms part of the actual cost of the asset and it should be capitalized in actual cost of the asset. Thus, the company would be allowed to capitalise the expenditure and claim a higher depreciation and investment allowance.
- (c) **Use of borrowing to finance purchase of fixed assets:** The company should also plan the optimum use of the share capital and the borrowed funds. Note that the borrowings should be utilised as far as possible for the acquisition and installation of assets like buildings, plant and machinery so that interest can be capitalised for the period after setting up of the acquired assets like buildings, plant and machinery but before the commencement of production. The interest and higher amount of depreciation (due to capitalisation of expense) may be claimed as revenue expenditure pertaining to the business of the company.
- (d) **Purchase of depreciable asset from borrowings or on hire:** The company should also plan to purchase the depreciable assets on credit terms and an agreed amount of interest can be paid on such credit purchases or the company may purchase these company assets on the basis of the hire purchase agreement enabling the company to claim the amount of interest paid as revenue business expenditure. The company would also be entitled to claim either the depreciation for use of the asset or may treat the hire charges as the rent for the asset in the normal course of business and claim deduction on revenue account.
- (e) **Taking the source of finances i.e. Capital or borrowings, the comparison between pre-commencement period and post commencement period is as follows:**
 - (a) (i) Dividend is not deductible either for pre commencement period or in the post commencement period in India;
 - (ii) Interest is capitalised for pre-commencement period, i.e. added to the cost of project (cost of fixed assets) and its depreciation is calculated on capitalised value of assets. In post commencement period, interest is fully deductible.
 - (b) (i) Cost of raising finance in case of capital is not deductible as revenue expenditure but amortised under Section 35D of the Act. If such expenditure is incurred after the commencement of the business, Section 35D is applicable provided the expenditure is undertaken for expansion purposes in case of industrial undertaking.
 - (ii) Cost of borrowing funds in case of pre commencement period is capitalised and in case of post commencement period, it is deductible fully in the year.

The above consideration will go a long way in suggesting the managements of corporate entities to adopt a suitable capital structure and selecting the appropriate financing sources by providing an optimal capital mix for the organisation.

Illustration

What are tax benefits available, where the asset is acquired on lease or purchase by own fund.

Solution**Purchase vs. Lease**

- (i) In case of purchase, depreciation is allowed under Section 32, while depreciation will not be allowed u/s 32 in case of Lease.
 - (ii) In case of Lease, revenue expenditure i.e., lease rent will be allowed as deduction u/s 37(1). Repairs are also allowable under Section 31.
- In case of Purchase, Insurance Premium, Current repairs are allowed as deduction u/s 31. Further, Interest on borrowed funds is deductible under section 36.
- (iii) Purchase of machinery would create a tangible asset which can also be mortgaged in the hours of need. While it is not so in case of Lease.

Illustration

A Ltd. wants to acquire a machine on 1st April, 2013. It will cost ₹ 1,50,000. It is expected to have a useful life of 3 years. Scrap value will be ₹40,000. If the machine is purchased through borrowed funds, rate of interest is 15% p.a. The loan is repayable in three annual instalments of ₹50,000 each. If machine is acquired through lease, lease rent would be ₹60,000 p.a.

Profit, before depreciation and tax is expected to be ₹ 1,00,000 every year. Rate of depreciation is 15%. Average rate of tax may be taken at 33.99%.

A Ltd. seeks your advice whether it should:

- (i) Acquire the machine through own funds, or borrowed funds; or
- (ii) Take it on lease.

Advice whether asset should be taken on lease or on purchase. Whether it should be acquired through own funds or borrowed funds? Present value factor shall be taken @ 10%.

Solution

In all the scenarios, profit is same, therefore, we can advice on the basis of present value of Outflow and loans.

(I) PURCHASING MACHINE**(i) Through own Funds**

Particulars	Year	(Amount in ₹)		
	0	1	2	3
Cash Outflow	(1,50,000)	–	–	–
Less: Tax Relief on Depreciation@33.99% (Rounded Off)	–	7,650	6,500	5,525

Less: Sale Proceeds of machine	—	—	—	40,000
Total	(1,50,000)	7,650	6,500	45,525
Present value Factor @10%	1	0.909	0.826	0.751
Present Value of Cash Outflows	(1,50,000)	6,954	5,369	34,189
Net Present Value of Cash Inflows (–) Outflows	₹(1,03,487)			

(ii) Through Loan Funds

Particulars	Year				(Amount in ₹)
	0	1	2	3	
<i>Cash Outflows:</i>					
Loan repayment		(50,000)	(50,000)	(50,000)	
Interest Payment		(22,500)	(15,000)	(7,500)	
<i>Cash Inflow</i>					
Less: Tax Relief on Depreciation/Loss @ 33.99%		7,650	6,500	5,525	
Less: Tax Relief on Interest		7,650	5,100	2,550	
Sale Proceeds of machinery	—	—	—	40,000	
Total		(57,200)	(53,400)	(9,425)	
Discounting factor @ 10%	1	0.909	0.826	0.751	
Present Value of Cash outflows (₹)	Nil	(51,995)	(44,108)	(7,078)	
Net Present Value of Cash Outflows	₹(1,03,181)				

(II) ACQUIRING MACHINE ON LEASE

Particulars	Year				(Amount in ₹)
	0	1	2	3	
<i>Cash Outflow on Lease rent:</i>	—	(60,000)	(60,000)	(60,000)	
Less: Tax Relief on Lease Rent @ 33.99%	—	20,390	20,390	20,390	
Net Cash Outflow		(39,610)	(39,610)	(39,610)	
Discounting factor @ 10%	1	0.909	0.826	0.751	
PV of Cash Outflows	—	(36,005)	(32,718)	(29,747)	
Net Present Value of Cash Outflows	₹(98,470)				

Conclusion: Cash outflow is least if machine is acquired on lease. Hence, machine shall be acquired on lease.

Working Notes:

Calculation of Tax relief on Depreciation and Balancing Allowance

Year	Opening Balance	Depreciation @ 15%	Tax Relief @33.99%
1	1,50,000	22,500	7,650

2	1,27,500	19,125	6,500
3	1,08,375	16,257	<u>5,525</u>
			<u>19,675</u>

TAX PLANNING RELATING TO NON-RESIDENTS

Suggested tax planning measures for Non-residents(NRs) are:

- (a) **Indian citizen coming to India for visit purposes:** As a NR is not required to pay tax on his income earned and received outside India, an Indian citizen having an assignment abroad could plan his visits to India in such a way so that he could remain to be a NR for the purposes of the Act. This is generally of interest to persons employed in foreign countries.
- (b) **Agents to retain sufficient money of NR to meet its tax liability in India:** All those dealing with NRs must keep in view the provisions of Sections 162 and 163. They should retain sufficient amounts with them to be paid on behalf of the NR towards his tax liability, so that they are not obliged to pay such taxes on their own account.
- (c) **NR to be aware about tax deduction by Agent to plan accordingly:** A NR must be very clear as regards his tax liability through agent. He must be aware that the agent will deduct some amount out of the amount payable to the NR.
- (d) **Person who could be treated as agent of NR:** Persons employed by or on behalf of a NR, those who have a business connection with NR and statutory agents are all considered as authorised agents of a NR. Even a NR could be treated as the agent of another NR.
- (e) **Tax paid by Agent is a dead loss if not recovered from NR:** It should be remembered that if the agent is unable to recover from the NR the amount of tax paid on his behalf, he cannot claim it as a bad debt or as business loss in view of SC decision in *CIT v. Abdullaabhai Abdhulkadar* (41 ITR 545).
- (f) **Business connection due to close financial association between a resident and a NR:** Another very important point is the close financial association between a resident and a NR. This can also amount to a business connection. In a case where all Indian banks and a foreign bank were controlled by the same persons and the main function of the foreign bank was to finance the Indian Bank, it was held that a business connection existed in India between the two banks. *Bank of Chettinad Ltd. v. CIT Madras* (PC) (8 ITR 522).
- (g) **Tax planning by Individuals to become NR in India:** Following persons may be treated as NR in India if their stay in India is less than 182 days during relevant previous year:
 - (i) an Indian citizen who has gone for employment purposes outside India during relevant previous year;
 - (ii) an Indian citizen who is a crew member of a foreign ship;
 - (iii) an Indian citizen coming to India during relevant previous year for visit purposes.
 - (iv) a person of Indian origin (a person who himself or his parents or his grandparents were born in undivided India) coming to India during relevant previous year for visit purposes.

Thus, in case of above mentioned persons, salary income earned abroad will not be taxed in India.

Above-mentioned persons may come on a visit to India during vacation for 181 days or less, or else if he desires to stay in India for a period longer than 181 days the visit should be so planned over two previous years that his total stay in any one previous year should remain 181 days or less. In this way, they can stay upto a total of 342 days at a stretch without becoming resident in any of the previous years.

Illustration

Tara, an Indian citizen, joined CIMA as a professor in UK on monthly salary of £8,000 on 1st October, 2002. She wants to proceed to India for a period of 11 months to get her own house constructed in Mumbai. Suggest the dates as to how she should plan her 11 months to India during 2013 and 2014 so that her salary and other foreign Income earned in London remain totally exempt in India.

Solution

The period of 11 months may be staggered over 2 years from 15th October 2013 to 15th September, 2014. Hence, in such a way the basic condition for residence is not satisfied.

Moreover, Tara can stay in India upto 362 days at a stretch (spread over two calendar years: 181 days in 2013 and 181 days in 2014) without becoming resident in any of the year.

TAX PLANNING FOR INDIAN COLLABORATORS

While entering into an agreement for foreign collaboration, the Indian collaborator should take into consideration such aspects as will enable him to plan his tax affairs in a manner that ensures maximum after tax profits and return on investment.

In this context, the Indian collaborator may be advised to adopt the following steps for tax planning:

(a) Capitalisation of Installation expenses:

As far as purchase of capital goods from the foreign collaborator is concerned, it is needless to say that this is a capital expenditure on which depreciation is admissible. Care should also be taken to see that the cost of installation, including the supervision expenses charged by the collaborator, is also capitalised and depreciation claimed thereon.

Indian company should also be vigilant that the other expenses relating to the collaboration agreement must be incurred after the date of setting up of the business, because only then it would be entitled to be capitalised as other expenses.

(b) Treating purchase of spares as revenue expenditure:

For the purchase of spares for the plant, the Indian collaborator should plan to receive the spares subsequent to the year of commissioning of the plant and preferably execute a separate contract in this behalf. It will enable the Indian company to treat the whole of the amount of spares as revenue expenditure.

In this context, the judgement of the Madras High Court in *CIT v. Rama Sugar Mills Ltd.* (21 ITR 191) is worth-noting. A sugar manufacturing company had three boilers at its factories. Two of these were constantly in use and the third one was kept as "spare" ready to be used when one of the other two boilers had to be cleaned up at intervals. The productive capacity of one of the boilers deteriorated and the company was required to purchase the other at a cost of ₹85,000. The Madras High Court held that this expenditure was deductible on revenue account, on the ground that "the boiler which was substituted was

exactly similar to the old one and by this expenditure, the assessee company did not bring any additional advantage to the trade or business, which they were carrying on and there is no improvement. It cannot be suggested that by using a new boiler for an old one, the production capacity of the sugar manufacturing unit was in any manner increased".

(c) Treating plans and drawings etc. as Plant for availing full value as depreciation:

In view of the Supreme Court's decision in the case of *CIT v. Alps Theatre* (65 ITR 177) Plant includes ships, vehicles, books, scientific apparatus and surgical equipments used for the purpose of business or profession. However, know how acquired on or after 1.4.1998, owned wholly or partly by the assessee and used by such assessee for the purpose of his business or profession, will form a separate block of asset alongwith other intangible asset and will be eligible for depreciation under Section 32(1) @ 25% on written down value.

TAX PLANNING FOR EMPLOYEES

The employees should keep the following aspects in view while planning their salary package:

- (a) Division of salary into basic pay and allowances: The employee should opt for division of salary into basic pay and allowances and should not opt for the consolidated salary as some allowances are exempt to the extent provided under section 10 of the Act e.g. House rent allowance, Transport allowance, Uniform allowances, Children education allowance.
- (b) Dearness allowance should be forming part of salary: Under the terms of employment, dearness allowance should form part of the retirement benefits. This will not only increase the employees retirement benefits but also reduce his tax incidence in respect of HRA, gratuity, commuted pension, employer's contribution to RPF, etc.
- (c) Commission to be based on turnover: Any commission payable as per the terms of employment should be based on turnover so as to form part of salary. This will also reduce the tax incidence in respect of HRA, commuted pension, interest credited to RPF.
- (d) Cubic capacity of more than one car for private use not to exceed 1.6 Litre: If the employee is allowed the use of more than one car for his private purposes, the horse power of any such car should not exceed 1.6 litre cubic capacity as otherwise he shall be deemed to have been provided with one car of 1.6 cubic litre capacity which would lead to higher valuation of such perquisite.
- (e) Employer's contribution to RPF exempt upto 12% of salary: The employer's contribution to RPF should be 12% of salary as it is exempt upto this limit.
- (f) Medical facility instead of medical allowance: The employee should opt for reimbursement of expenses on medical treatment (or free medical facility) in place of medical allowance because such allowance is fully taxable whereas the reimbursement is not taxable upto the extent of ₹15,000.
- (g) Perquisites in preference to taxable allowances: Perquisites should be preferred to taxable allowances. This shall help not only in lower valuation of a perquisite like rent free house but the employee will also be free from falling into the category of specified employees.
- (h) Use of furniture not taxable in case of non specified employee: It may be noted that if furniture is provided without rent free accommodation, it will not be taxable in the hands of non specified employees.
- (i) RPF maintained in the enterprise of subsequent employers: An employee who resigns before completing five years of continuous service in an organisation, should ensure that the new organisation he joins maintains RPF so that the accumulated balance of the provident fund could be transferred to the new organisation to claim exemption thereon.

- (j) Preference should be for commuted pension on retirement: On retirement, the employee should opt for commuted pension to the maximum permissible limit as it is exempt from tax within certain limits.
- (k) Leave encashment should be received on retirement: Leave encashment should preferably be done on termination of employment by superannuation or otherwise as it will then be exempt from tax within certain limits.
- (l) Avail permissible deductions under Chapter VIA: The employee should also plan for taking full advantage of the relevant provisions under Section 80C to 80U of the Act.

Illustration

A company is paying following remuneration to an employee in Delhi who was earlier employed in Mumbai.

- (i) *Salary: ₹20,000 p.m.*
- (ii) *Conveyance Allowance: ₹ 2,000 per month*
- (iii) *Education Allowance of ₹ 600 p.m. for his children*
- (iv) *Establishment and upkeep allowance of ₹ 5,000 per month*
- (v) *Entertainment allowance of ₹ 10,000 per month*
- (vi) *Medical expenses upto ₹ 10,000 p.a are reimbursed upon submission of medical bills.*
- (vii) *Employee is married and has two children. He has been paid a leave travel allowance of ₹ 5,000 for going to Kashmir.*

Consider the tax implication both from the point of view of the company and the employee. You are required to suggest a method which will bring the minimum advantage both to the company as well as employee.

Solution

Tax implications for components of salary are as under:

From viewpoint of Employee:

- (i) *Salary: It is taxable under Section 17(1) of the Act.*
- (ii) *Conveyance Allowance: Employee is entitled to claim exemption of ₹800 pm towards conveyance allowance.*
- (iii) *Education Allowance: Employee is entitled to claim exemption under Section 10(iv)(ii) read with Rule 2BB and maximum exemption is upto ₹100 per month per child for maximum of 2 children.*
- (iv) *Entertainment Allowance: It is fully taxable in employee's hands.*
- (v) *Establishment and Upkeep Allowance: It is fully taxable for an employee under Section 17(2).*
- (vi) *Medical Expenses Reimbursement: It is exempt upto ₹15,000 for an employee amount reimbursed beyond ₹15,000 will be taxable.*
- (vii) *Leave Travel Allowance: It is wholly taxable Section 10(5) applies to reimbursement but not to a fixed allowance.*

From the viewpoint of Employer:

Employer will get the deduction under Section 37(1) for the following:

- (i) *Salary:*

Note: For claiming deduction, salary should be provided after commencement of business.

If it is incurred prior to commencement of business, it should relate to scientific research relating to business within 3 years prior to its commencement under Section 35(1).

- (ii) Conveyance Allowance
- (iii) Education Allowance
- (iv) Entertainment Allowance
- (v) Establishment and Upkeep Allowance
- (vi) Medical expenses and reimbursement
- (vii) Leave Travel Allowance

Tax Planning:

- (a) *Entertainment Allowance*: Expenditure incurred by an employee in entertaining company's customers or for official purposes should be reimbursed to him to avoid his tax liability.
- (b) *Education Allowance*: Instead of education allowance, education facility should be provided. Education facility is not taxable in the hands of an employee who is non-specified. For a specified employee, the company is suggested to evolve a scheme of scholarship based on merit. It is not an Income of Employee. Employer may claim deduction u/s 37(1). Also, employee is entitled to claim exemption upto ₹100 per month per child.
- (c) *Medical Expenses*: Instead of medical allowance, reimbursement for medical expenses should be provided as medical allowance is fully taxable while medical reimbursement is exempt upto ₹ 15,000.
- (d) *Establishment and Upkeep Allowance*: This allowance can be given under the name of House Rent allowance to an employee so as to enable him to claim exemption under Section 10(13A) read with Rule 2A. Employer is entitled to claim deduction under Section 37(1).
- (e) *Leave Travel Concession*: The company is advised to grant leave travel concession or reimbursement to enable the employees to seek exemption under Section 10(5) instead of Leave Travel allowance which is fully taxable.
- (f) *Retirement Benefit Scheme*: The Company is advised to introduce retirement benefit scheme, i.e., Introduction of Recognized Provident Fund (RPF). Employer's contribution is deductible u/s 36 read with Section 43B. Employee gets deduction u/s 80C. Repayment at retirement is exempt if employee has served 5 years or more.

Illustration

Arun is employed with P Ltd. at a salary of ₹ 40,000 per month. He is also paid House rent allowance of ₹ 10,000 per month. His wife, Tannu is also employed at a salary of ₹ 20,000 per month with G Ltd. where Arun holds 20% shares. Tannu does not hold adequate qualification for the post which she is holding. Tannu is the owner of a house, which is self occupied by the family. Municipal value of house is ₹ 3,00,000. The house was constructed in the year 2013-14 with borrowed funds. Interest on loan is payable of ₹ 1,75,000 p.a. Tannu has insured the house and paid insurance premium of ₹5,000 to National Insurance Company. Tannu has also paid ₹15,000 as Municipal taxes.

Arun pays insurance premium of ₹26,000 for himself, his wife and two children. He also pays school fees of ₹24,000 for the children.

Suggest a scheme of tax planning to minimize the tax liability during the financial year 2013-14.

Solution:**Tax Planning:**

- (i) Arun is advised to reduce his shareholding with G Ltd. from 20% to 19% to avoid clubbing of salary income of Tannu (Arun's wife) under Section 64(1)(ii).
- (ii) Tannu should not treat the house as self occupied. She should let it out to Arun and issue a rent receipt of an amount say ₹20,000 per month.

On the basis of rent receipt, Arun is entitled to claim the exemption in respect of house rent allowance to reduce his tax liability. Besides, she can claim full deduction in respect of interest payable on housing loan, whereas she can claim maximum deduction of ₹1,50,000 for such interest when the house is self occupied for residence.

TAX PLANNING UNDER WEALTH TAX ACT

As measures of tax planning, companies can take the following precautions:

- (a) **Avoid Investment in taxable assets:** As far as possible, companies should avoid to invest in taxable assets like jewellery, motor cars, other unproductive assets etc.
- (b) **Investment in taxable assets, if required, to be done from borrowed funds:** In unavoidable cases, the investment in the said assets could be made out of loan or a debt may be incurred in relation thereto, by way of furnishing a security for a loan. For example, companies generally finance the purchase of assets like, motor cars/trucks/vehicles etc. through bank loans/overdrafts/mortgage.
- (c) **Purchase of house property by a company for employee to be out of borrowed funds:** Likewise, purchase of a house property likely to be used by the Directors/Manager/Secretary as their residential accommodation or by any other employee who has a substantial interest in the company (holding at least 10% equity shares of the company) could be funded out of loan/raising of debts thereon.

This strategy will help the company to dilute the incidence of tax on its wealth.

PLANNING IN THE CONTEXT OF COURT RULINGS AND LEGISLATIVE AMENDMENTS

The tax planner while planning his affairs or that of his clients must take into account not only the relevant legal provisions, but also the judicial pronouncements of Appellate Tribunals, High Courts and Supreme Court. He should also take into consideration all relevant rules, notifications, circulars etc.

As for circulars, since they are in the nature of administrative or executive instructions, the possibility that they might be withdrawn by the CBDT (Board) at any time, should also be taken into account. They may be challenged in the courts although, otherwise they are binding at the administrative level. In cases where the circulars are based on an erroneous or untenable footing, they are liable to be quashed by the Courts.

LEGISLATIVE AMENDMENTS

It is a common feature of modern legislative system to lay down in the Acts, the principles and the policy of the legislature leaving out details to be filled in or worked out by rules or regulations made either by the Government or by some other authority as may be empowered in the legislations.

This kind of subordinate or administrative legislation is justified and even necessitated by the fact that the legislature has neither the time nor the material to consider and act with reference to various details.

Section 295(1) of the Income-tax Act and Section 46(1) of the Wealth tax Act respectively vest in the Central Board of Direct Taxes (CBDT) the power to give retrospective effect to any of the rules in such a way as not to prejudicially affect the interest of the tax payers.

The various matters in respect of which the rules may be framed are specified in the relevant sections. Section 119 read together with Section 295 empowers CBDT to frame rules, issue circulars, notifications, administrative instructions to the subordinate authority for smooth functioning of the Income-tax Act, 1961. Section 119 read together with Section 295 gives general powers to CBDT to frame the rules and notifications. However, relevant sections empower CBDT to frame rules and issue relevant notifications. For example, Section 44AA provides that certain persons carrying on profession or business such as legal, medical, architectural or interior decoration or the profession of accountancy or technical consultancy or any other profession as is notified by the Board. Therefore, on careful perusal of Section 44AA, it may be seen that this Section empowers CBDT to issue notification to the effect that other professions shall be covered by the provisions of Section 44AA for maintenance of books of account.

STATUTORY FORCE OF THE NOTIFICATIONS

Section 296 of the Income-tax Act, 1961 provides that the Central Government shall cause every rule made under this Act or for that matter any notification issued, to place before both the Houses of Parliament either before issuing them or in case same is issued when Parliament is not in session, immediately thereafter when the Houses are in session.

Rules and notifications are made by the appropriate authority in exercise of the powers conferred on it under the provisions of the Act. Therefore, they have statutory force and can be equated to the law made by the legislature itself. Thus, they are a part and parcel of the enactment.

The rules cannot, however, take away what is expressly conferred by the Act. In other words, they cannot whittle down the effect of the law. If there is any irreconcilable conflict between a rule and a provision in the Act, the provision in the Act will prevail.

Notifications when validly made in exercise of the authority provided for in the law, are equally binding on all concerned and may be enforced. Section 119(1) of the Income-tax Act provides that all officers and other persons employed in the execution of the said Act shall observe and follow the orders, instructions and directions of the Board, provided that such orders, instructions or directions shall be issued as not to interfere with the discretion of the Appellate Commissioner in the exercise of his appellate functions.

In the case of *Collector of Central Excise v. Parle Exports (P) Ltd.* (183 ITR 624), the Supreme Court held that when a notification is issued in accordance with powers conferred by the statute, it has statutory force and validity and therefore, it is as if the exemptions under the notifications were contained in the Act itself.

Further, it is judicially settled that the circulars issued by the Board would be binding under Section 119 on all the officers and persons employed in the execution of the Act [*Navnital Javeri Sen v. CIT* (56 ITR 198) (SC)].

The Board is not competent to give directions where the exercise of any quasi judicial discretion by the subordinate authorities in individual cases is involved. [*J.K. Synthetics Ltd. v. CBDT* (1972) 83 ITR 335 (SC)].

It has been clarified by the Supreme Court in *Kerala Financial Corporation v. CIT* (210 ITR 129) that Section 119 does not empower the CBDT to issue order, instruction or direction overriding the provisions of the Act.

The various judicial rulings point out the following:

- (a) The instructions of the Board are binding on the Department but not on the assessee.

- (b) The instructions have to be followed by the Departmental Officers. Instruction adverse to an assessee's interest can be challenged by him.
- (c) The instructions withdrawn subsequently should be given effect to by the Assessing Officer for the assessment year for which they were in force even though they are withdrawn at the time he makes the assessment.
- (d) In the exercise of its power, the Board cannot impose a burden or put the assessee in a worse position.

ORGANISATION OF TAX PLANNING CELLS

Companies having effective tax planning cells (departments) can plan their transactions with a view to attract the least incidence of tax. Organisation of such a cell can be justified on the following grounds:

(a) Complexity and volume of work:

Where the volume of tax work to be handled is large and highly complex, then it is required to appoint a special tax expert along with the required staff.

(b) Separate Documentation:

Documentation is an indispensable ingredient of tax management. An assessee has to keep reliable, complete and updated documentation for all the relevant tax files so that the documentary evidence can be made available at a short notice whenever it is required. In absence thereof, an assessee may lose a case for want of proper documentary evidence.

(c) Data collection:

The staff concerned with taxation has to collect and keep on collecting data relating to latest circulars, case laws, rules and provisions, and other government notifications to keep abreast of the current developments. This could also guide them in any particular area, when such guidance is needed.

(d) Integration:

Tax planner should be consulted by all the departments of the company to know the impact of taxation on their decisions. It would be necessary to integrate and properly link all the departments of the company with the tax planning department. Any project or blue print may have a tax angle. This has to be identified early enough to facilitate better tax compliance and availing of the several incentives.

(e) Constant Monitoring:

In order to obtain the intended tax benefits, persons connected with tax management should ensure compliance of all the pre-requisites, like procedures, rules etc. Besides, there should be constant monitoring, so that all the tax obligations are discharged and penal consequences avoided.

(f) Developing tax effective alternatives:

A managerial decision could be assumed to have been well taken only if all the pros and cons are considered. A tax planner could guide important decisions, by considering varieties of alternatives and choices.

(g) Take advantage of various allowances and deductions:

A tax manager has to keep track of the provisions relating to various allowances, deductions, exemptions, and rebates so as to initiate tax planning measures.

LESSON ROUND UP

(These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.)

- Tax Planning may be legitimate provided it is within the framework of the law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid payment of tax by resorting to dubious methods.
- Tax planning, in fact, is an honest and rightful approach to the attainment of maximum benefits of the taxation laws within their framework.
- Tax planning can be of following types: Short and long range tax planning, Permissive tax planning and purposive tax planning.
- Some of the important areas where planning can be attempted in an organised manner are as under:
 1. **At the time of setting up of new business entity:**
 - (a) Form of organisation/ownership pattern;
 - (b) Locational aspects;
 - (c) Nature of business.
 2. **For the business entities already in existence:**
 - (a) Tax planning in respect of corporate restructuring;
 - (b) Tax planning in respect of financial management;
 - (c) Tax planning in respect of employees remuneration;
 - (d) Tax planning in respect of specific managerial decisions;
 - (e) Tax planning in respect of Foreign collaborations and Joint Venture Agreements;
 - (f) Tax planning in the light of various Double Taxation Avoidance Agreements (DTAA)
- The basic objectives of tax planning are: (a) Reduction of tax liability; (b) Minimisation of litigation; (c) Productive Investment; (d) Healthy growth of economy; (e) Economic Stability.
- Tax Avoidance will be used to describe every attempt by legal means to prevent or reduce tax liability which would otherwise be incurred by taking advantage of some provisions or lack of provisions of law. It excludes fraud, concealment or other illegal measures.
- Tax evasion is a method of evading tax liability by dishonest means like suppression, showing lower incomes, conscious violation of rules, inflation of expenses etc.
- The tax planner while planning his affairs or that of his clients must take into account not only the relevant legal provisions, but also the judicial pronouncements of Appellate Tribunals, High Courts and Supreme Court. He should also take into consideration all relevant rules, notifications, circulars etc.
- Organisation of tax planning cell can be justified on the grounds of (a) Complexity and volume of work (b) Separate documentation (c) Data collection (d) Integration (e) Constant monitoring (f) Developing tax effective alternatives (g) Take advantage of various allowances and deductions.

SELF TEST QUESTIONS

1. Specify whether the following acts can be considered as an act of (i) tax management; or (ii) tax planning; or (iii) tax evasion:
 - (a) A deposits ₹72,000 in PPF account so as to reduce tax payable.
 - (b) A Industries Ltd. installed an air conditioner costing ₹60,000 at the residence of a director as per terms of his appointment; but treats it as fitted in quality control section in the factory. This is with the objective to treat it as plant for the purposes of computing depreciation.

- (c) A Industries Ltd. maintains registers of tax deduction effected by it to enable timely compliance.
- (d) T Ltd. issues a credit note for ₹36,000 for brokerage payable to A, who is son of G, managing director of the company. The purpose is to increase his income from ₹18,000 to ₹54,000 and reduce its income accordingly.
- (e) A is a working partner in TA Industries. In such capacity, he is entitled to a salary of ₹7,500 per month. He treats this as salary instead of business income.
- (f) A is using a motor car for his personal purposes, but charges as business expenditure.
2. Explain the concept of tax planning and state its importance for a company.
 3. Explain the three methods by which an assessee can reduce his tax liability.
 4. Distinguish between tax evasion and tax avoidance.
 5. Explain the two schools of thought on tax avoidance. Enumerate the general principles regarding tax avoidance.
 6. What are the objectives of tax planning? Enumerate the requisites for its success.
 7. Discuss in detail the areas where the tax planning can be resorted to by an assessee.
 8. Compare the different forms of organisation from tax liability points of view.
 9. "All companies are not liable to wealth tax, even those which are liable have scope for minimising it." Comment.
 10. What is 'reverse mortgage'? Whether loan received under the scheme of reverse mortgage amounts to income in the hands of borrower? Whether mortgage of the property under reverse mortgage is treated as transfer so as to attract capital gains under section 45? Whether alienation of the mortgaged property by the mortgager for the purpose of recovering the loan would amount to transfer so as to attract capital gains under section 45?
 11. Examine whether the following are 'assets' under the provisions of the Wealth tax Act, 1957:
 - (a) A commercial complex;
 - (b) A building occupied by the assessee for business purposes;
 - (c) Aircrafts owned and used by the assessee for business purposes;
 - (d) Land owned by the assessee situated outside a municipality but within a notified area.
 - (f) Jewellery, bullion and utensils made of precious metals.

Answer/Hint:

1. (a) Tax planning; (b) Tax evasion; (c) Tax management; (d) Tax evasion; (e) Tax evasion; (f) Tax evasion
11. (a) Not an asset u/s 2(ea); (b) Not an asset u/s 2(ea); (c) Not an asset if used for commercial purposes; (d) Asset u/s 2(ea); (e) Asset u/s 2(ea).

Lesson 4

Indirect Tax Laws and Practice - an Introduction

LESSON OUTLINE

Introduction

Constitutional provisions in relation to taxation

Indirect taxes

- Central Excise Law
 - Limbs of central excise law
- Customs
- Provisional Collection of Taxes Act, 1931
- Service Tax
- Central Sales Tax
- Value Added Tax (VAT)
 - Methods of computation
 - Procedure
 - Rates of tax

Lesson Round Up

Self-Test Questions

LEARNING OBJECTIVES

The major form of levy of indirect taxes is in the nature of Excise Duty, Customs Duty, Service Tax, Central Sales Tax and Value Added Tax. Each of these duties or taxes has a basis or an incidence that justifies such levy. For instance, customs duty is levied on import and export of goods, while excise is a duty on manufacture of goods. The Central Board of Excise & Customs ("CBEC") is the apex regulatory body that supervises the levy and administration of indirect taxes in India.

In the recent years, the Indian government has undertaken significant reforms under indirect taxation system. This includes the initiation of a region-based and state-level VAT on goods, the Central Sales Tax, which obstructs easy trading between different states, is being under the process of termination that would help to abolish the control measures on the inter-state trade and Goods and Service Tax (not yet rolled out). For proper compliance of the indirect tax laws and cost minimization, Company Secretaries with their in-depth knowledge and wide-range experience can offer their professional services to the industry. For this, proper understanding of the Indirect tax subject is indispensable.

Central Board of Excise and Customs (CBEC) is a part of the Department of Revenue under Ministry of Finance, Government of India. The Board is the administrative authority for its subordinate organisations including Custom Houses, Central Excise and Service Tax commissionnerates and the Central Revenue Control Laboratory.

INTRODUCTION

Government requires funds for the purposes of carrying out its activities, which are mainly maintenance of law and order, defence, public policy etc. These funds are generated through revenue, which comes from corporate tax, Income Tax, Customs duty, Excise duty, other taxes etc. Major portion of the revenue of the country comes from taxes.

Taxes are classified as Direct Taxes and Indirect Taxes, Direct taxes are paid by taxpayer directly from his income/wealth etc. Whereas indirect taxes are paid by taxpayer indirectly i.e. he pays the same at the time of purchasing goods and commodities, paying for services etc. Important indirect taxes are Central Excise, Customs, Service Tax, Central Sales Tax and VAT. Out of these indirect taxes major contribution to the country's revenue is made by levy of excise duty and service tax for the Central Government. The revenue of Central Sales Tax & VAT will go to respective state government.

CONSTITUTIONAL PROVISIONS IN RELATION TO TAXATION

The Constitution of India is the supreme law. All other laws emanate from the Constitution. Articles 245 to 255 provide for the distribution of taxation powers between the Union and the States. It may be recalled at this stage that India is having a quasi-federal Constitution in which the powers of legislation are shared between the Union and the States.

- Union List: Parliament has exclusive power to make laws with respect to any of the matters enumerated in List I in the Seventh Schedule to the Constitution; this List is referred to usually as Union List.

Some of the major entries pertaining to indirect taxes:

Sl. No.	No. of Entry in the Seventh Schedule	Description
1	82	Taxes on income other than agricultural income.
2	83	Duties of customs including export duties.
3	84	Duties of excise on tobacco and other goods manufactured or produced in India except — (a) alcoholic liquors for human consumption; (b) opium, Indian hemp and other narcotic drugs and narcotics, but including medicinal and toilet preparation containing alcohol or any substance included in sub-paragraph(b) of this entry.
4	92A	Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of 'inter-State trade or commerce'.
5	92B	Taxes on the consignments of goods (whether the consignment is to the person making it or to any other person), where such consignment takes place in the course of inter-State trade or commerce.
6	92C	Taxes on services (Not yet notified)
7	97	Any other matter not enumerated in List II or List III including any tax not mentioned in either of those Lists.

As the Entry No. 92C not yet notified therefore, till date Service Tax is levied under Entry No. 97.

- **State List:** The legislature of every State has exclusive power to make laws for such State or any part thereof with respect to any of the matters enumerated in List II in the Seventh Schedule to the Constitution. This list is popularly called as State List. VAT is imposed under Entry 54 of state list.

INDIRECT TAXES

In this study we will discuss the following types of indirect taxes:

1. Central Excise law
2. Customs Law
3. Service Tax
4. Value Added Tax
5. Goods and Service Tax (Proposed to be rolled out)

Let's discuss in brief the history and developments taken place in above mentioned taxes:

CENTRAL EXCISE LAW

Central Excise law is governed by Central Excise Act, 1944, Central Excise Tariff Act, 1985 and rules made there under. The Central Excise duty is administered by the Central Government under the authority of Entry number 84 of the Union List (List I) under Seventh Schedule read with Article 246 of the Constitution of India.

History and Legislative background*

After independence, excise duties were levied on selected goods but over the years, as the revenue requirement increased, the list of commodities subject to duty was expanded. Further for reasons of administrative convenience, the duties were levied on raw material and intermediate goods rather than final consumer goods. In the year 1975–76 the ambit of the duty was extended to all manufactured goods.

There were two ways of levying the commodities either levy a specific duty or *ad valorem* duty and the later one had 24 different rates varying from 2 to 100 per cent (excluding tobacco and petroleum products which were taxed at higher rates). The Indirect Tax Enquiry Committee recommended for conversion of specific duties into *ad valorem*, unification of duty rates and introduction of input duty credit to convert the duty into a Manufacturing stage Value Added Tax (MANVAT) to curb the cascading effect of tax as levied on inputs, capital goods as well as on final consumer goods. The process of converting specific duties to *ad valorem* rates was more or less completed by 1993–94 and side by side the coverage of the credit mechanism also evolved over time. It began with selected items, with credit based on a one-to-one correspondence between inputs and outputs. It was only by 1996–97, that it covered a majority of commodities.

The recommendation of Tax Reform Committee brought wide ranging excise duty reforms. In the year 1999–2000, 11 tax rates were merged into three tax rates along with two other rates on luxury items. Further these three rates were merged into a single rate in 2000–01 to be called a Central VAT (Cenvat), along with three special additional excise duties of 8, 16, and 24 percent for a few commodities.

At present, as there are two schedules in Central Excise Tariff Act, 1985, the duty under first schedule attracts CENVAT at 12% for majority of the products and Special Excise Duty (SED) levied additionally on Schedule II goods is exempt.

* Trends and Issues in Tax Policy and Reform in India by M. Govinda Rao & R. Kavita Rao, National Institute of Public Finance and Policy, New Delhi

Limbs of Central Excise Law

- Central Excise Act, 1944
- Central Excise Tariff Act, 1985
- Central Excise Rules, 2002
- Cenvat Credit Rules, 2004
- Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000
- Central Excise (Determination of Retail Sale Price of Excisable Goods) Rules, 2008
- Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001
- Central Excise (Advance Rulings) Rules, 2002
- Central Excise (Appeals) Rules, 2001
- Central Excise (Compounding of Offences) Rules, 2005
- Customs and Central Excise Duties and Service Tax Drawback Rules, 1995
- Central Excise (Removal of Difficulties) Rules, 2005
- Central Excise (Settlement of Cases) Rules, 2007
- Consumer Welfare Fund Rules, 1992
- Customs, Excise & Service Tax Appellate Tribunal (Procedure) Rules, 1982
- Pan Masala Packing Machines (Capacity Determination And Collection of Duty) Rules, 2008
- Chewing Tobacco and Unmanufactured Tobacco Packing Machines (Capacity Determination and Collection of Duty) Rules, 2010
- Clean Energy Cess Rules, 2010 or other rules.

CUSTOMS LAW

Customs duties date back to 18th century when the British East India Company virtually came to political power in India. The three Presidencies namely Bengal, Mumbai and Chennai had their own customs regulations. Until 1859, there was a uniform all India tariff. The tariff underwent important changes in 1867, 1870, 1894, 1932, 1934 and 1939. After independence a major change was effected in 1975 when Customs Tariff was aligned with the Customs Cooperation Council Nomenclature (CCCN) which is the internationally accepted classification. In 1985, the Customs Cooperation Council developed a new system of nomenclature known as the harmonized commodity description and coding system. India also adopted this system by making an amendment to the Customs Tariff Act, 1975, by substituting a new Customs Tariff Schedule. As in the case of central excise, in the case of custom also, the levy is specified in the Customs Act, 1962 whereas the detailed classification of goods is given in the Customs Tariff Act, 1975.

In addition, under the Custom Tariff Act, 1975 additional duties of customs, popularly called *countervailing duty* (CVD) is also levied on goods imported into India with a view to protecting the indigenous industry, the duty is equivalent to the duty of excise on such imported goods if manufactured in India. Customs duties are basically duties on goods imported into India, in comparison to excise duties which are basically duties on goods manufactured or produced in India. This duty is imposed under Section 3(1) and 3(3) of Customs Tariff Act, 1975.

Besides the CVD as above, Special CVD (also known as SAD) is imposed under Section 3(5) of the Customs Tariff Act, 1975. This additional duty of Customs is in lieu of Sales Tax which is charged at a fixed rate of 4%.

Customs Act, 1962 and Custom Tariff Act, 1975 are the two major Acts governing the subject of Customs. These are supplemented by various set of Rules, Regulations Notifications ,circulars etc.

Protective duties may also be imposed under Tariff Act. They are :

- (i) Protective duty.
- (ii) Safeguard duty
- (iii) Anti subsidy duty
- (iv) Anti dumping duty.

PROVISIONAL COLLECTION OF TAXES ACT, 1931

Provisional Collection of Taxes Act, 1931 applicable to excise and customs. Only. Any duty imposed or increased in the budget will have immediate effect if the Finance Minister makes any declaration to that effect on the budget day in the parliament. But any decrease or reduction of duty will have effect only after the finance bill is passed, i.e. Finance Bill becomes Finance Act.

The declaration made under this Act will expire on 75th day from the date of introduction of bill if the bill is not passed by parliament.

If the increased duties are reduced / rejected by parliament while passing the finance bill, then the excess amount collected will be refunded.

SERVICE TAX

As the economy grows and develops, the contribution of the services sector becomes more substantial. Hence, tax on services becomes substantial revenue for the Government. Although Service tax is a concept of the modern era where developed economies as well as developing economies find over 70% of their gross economic output coming from the service sector. Service tax was there in vogue even in the Mauryan period in India. *Ms. Romila Thapar* in her “*Asoka and the Decline of the Mauryas*”, at page 72 (London 196, paperback edition, 1997, by Oxford) points out that services of weapon and implement makers were required to be provided to the state for a certain number of days in a year. This was a form of service tax in that period. But in the modern context, because of the increasing contribution of the service sector to the GDP of an economy, the importance of service tax is growing. As under the WTO agreements governments are required to reduce customs tariffs, governments are considering increase in service taxes revenues as a compensatory revenue generation mechanism. In terms of economics, tax on services is an indirect tax. This is because the burden of service tax can be passed on to the customer i.e., the recipient of the service. The service provider may also bear the burden of the tax by not passing or charging the same to a customer.

The Tax Reforms Committee headed by *Dr. Raja J Chelliah* recognized the revenue potential of the service sector and recommended imposition of service tax on selected services (selective approach or positive list approach). Consequently the service tax was imposed at a uniform rate of 5% in the Union Budget for 1994-95 on 3 services.

Finance Act, 2012 has made remarkable changes in service tax legislation whereby the concept of Positive list of Taxable services has been replaced with a negative list. A negative list of services implies that there is, a list of services which are not be subject to service tax. Service tax will not be chargeable on the services

mentioned in the negative list and which are exempted by issue of notification. This is in contrast to the earlier method of taxation of services where the law had provided definition for each taxable service and all other undefined services were outside the preview of Service Tax.

CENTRAL SALES TAX

As regards sales-tax both the Union and the States have the power to levy sales-tax. Under entry 92A of the Union list, the Union Government has power to levy taxes on the sale or purchase of goods other than newspapers where such sale or purchase takes place in the course of inter-State trade or commerce. Under Entry 54 of the States List the States have power to levy tax on sale or purchase of goods other than newspapers subject to the provisions of Entry 92A of the Union List. Under Article 286(1) of the Constitution a State can not impose any tax on sale or purchase of goods where such sale or purchase takes place:

- (a) outside the State;
- (b) in the course of import into or export of goods out of territory of India.

In other words, the powers of the State Governments to levy sales tax is restricted to sales within the State only. All inter-State sales are subject of Union's jurisdiction. Similarly all sales in the course of import or export are within the jurisdiction of the Union of India.

As regards the State sales taxes, each and every State has necessary powers to introduce tax on sales or purchase of goods, by separate State enactments. It is not possible to say that the various sales tax laws of different State Governments in India are uniform. They differ in many respects. To ensure uniformity and also to avoid unwarranted competition among the states, VAT has been introduced all over India. This is a major development in indirect taxes in recent times.

Under the Central sales-tax law which is within the purview of the Union legislature, tax is levied on inter-State sales only. If a transaction is proved to be an inter-State sale it ceases to be a local sale for a particular State. For the sake of convenience the State sales tax authorities have been conferred the power to collect the central sales-tax also.

All sales tax matters, be it central sales tax or state sales tax, are administered by respective state governments. Even the taxes collected on interstate sale are retained and utilized by the states.

VALUE ADDED TAX (VAT)

The Value Added Tax (VAT) in India is a state level multi-point tax on value addition which is collected at different stages of sale with a provision for set-off for tax paid at the previous stage i.e., tax paid on inputs. It is to be levied as a proportion of the value added (i.e. sales minus purchase) which is equivalent to wages plus interest, other costs and profits. It is a tax on the value added and can be aptly defined as one of the ideal forms of consumption taxation since the value added by a firm represents the difference between its receipts and cost of purchased inputs. Value Added Tax is commonly referred to as a method of taxation whereby the tax is levied on the value added at each stage of the production/distribution chain. As against the existing regime under which goods are charged to tax at Single point, or multi-point on the value of the goods, without any credit being given for taxes paid at the preceding stages. VAT intends to tax only the value added at each stage and not the entire invoice value of the product. By ensuring that only the incremental value is taxed, VAT aims at eliminating the cascading effect of taxes on commodities, and thereby reduces the eventual cost to the consumer.

It is one of the most radical reforms, albeit only in the sphere of State level taxes on sale, those have been initiated for the Indian economy after years of political and economic debate aiming at replacing complicated tax structure to do away with the fraudulent practices.

With the objective to introduce State-Level VAT in India in the Year 1992, the Government of India constituted a Tax Reform Committee headed by *Dr. Raja J. Chelliah*. In 1993, the Committee recommended the introduction of VAT in place of existing tax system. Thereafter, the Government appointed NIPFP (National Institute of Public Finance and Policy), New Delhi, as the Nodal Agency to work out the modalities of VAT.

The first preliminary discussion on State-Level VAT took place in a meeting of Chief Ministers convened by Dr. Manmohan Singh, the then Union Finance Minister in 1995. In this meeting, the basic issues on VAT were discussed in general terms and this was followed up by periodic interactions of State Finance Ministers.

For implementing the above decisions, an Empowered Committee of State Finance Ministers was set-up. Thereafter, this Empowered Committee met frequently and got full support from the State Finance Ministers, the Finance Secretaries and the Commissioners of Commercial Taxes of the State Governments as well as Senior Officials of the Revenue Department of the Ministry of Finance, Government of India. Through repeated discussions and collective efforts of all, it was possible to achieve remarkable success within a period of about one and half years. After reaching this stage, steps were initiated for the systematic preparation for the introduction of State-Level VAT.

Along with these measures ensuring convergence on the basis issues on VAT, steps were taken for necessary training, computerization and interaction with trade and industry, particularly at the State level. This interaction with trade and industry was specially emphasized. The conference of State Chief Ministers presided over by Shri Atal Behari Vajpayee, the then Prime Minister, held on October 18, 2002 at which Shri Jaswant Singh, the then Finance Minister was also present, confirmed the final decision that all the States and the Union Territories would introduce VAT from April 1, 2003.

A White Paper on State-Level Value Added Tax (VAT) by The Empowered Committee of State Finance Ministers (Constituted by the Ministry of Finance, Government of India on the basis of Resolution Adopted in the Conference of the Chief Ministers on November, 16, 1999, New Delhi, January 17, 2005. The Empowered Committee in the White Paper has justified the introduction of VAT in the following words:

“In the existing sales tax structure, there are problems of double taxation of commodities and multiplicity of taxes, resulting in a cascading tax burden. For instance, in the existing structure, before a commodity is produced, inputs are first taxed, and then after the commodity is produced with input tax load, output is taxed again. This causes an unfair double taxation with cascading effects. In the VAT, a set-off is given for input tax as well as tax paid on previous purchases. In the prevailing sales tax structure, there is in several states also a multiplicity of taxes, such as turnover tax, surcharge on sales tax, additional surcharge, etc. With introduction of VAT, these other taxes will be abolished. In addition, Central Sales Tax is also going to be phased out. As a result, overall tax burden will be rationalized, and prices in general will also fall. Moreover, VAT will replace the existing system of inspection by a system of built-in self-assessment by the dealers and auditing. The tax structure will become simple and more transparent. That will improve tax compliance and also augment revenue growth..... The VAT will therefore help common people, traders, industrialists and also the Government. It is indeed a move towards more efficiency, equal competition and fairness in the taxation system”.

The first preliminary discussion on State-level VAT took place in a meeting of Chief Ministers convened by Dr. Manmohan Singh, the Union Finance Minister in 1995. In this meeting, the basic issues on VAT were discussed in general terms and this was followed up by periodic interactions of States Finance Ministers. Thereafter, in a significant meeting of all Chief Ministers, convened on November 16, 1999 by Shri Yashwant Sinha, the then Union Finance Minister, three important decisions were taken. First, before the introduction of State-level VAT, the unhealthy sales tax rate “war” among the States would have to end and sales tax

rates would need to be harmonized by implementing uniform floor rates of sales tax for different categories of commodities with effect from January 1, 2000. Second, in the interest again of harmonization of incidence of sales tax, the sales-tax-related industrial incentive schemes would also have to be discontinued with effect from January 1, 2000. Third, on the basis of achievement of the first two objectives steps would be taken by the states for introduction of State-level VAT after adequate preparation. For implementing these decisions, an Empowered Committee of State Finance Ministers was set-up.

Thereafter, this Empowered Committee has met regularly, attended by the state Finance Ministers, and also by the Finance Secretaries and the Commissioners of Commercial Taxes of the State Governments as well as senior officials of the Revenue Department of the Ministry of Finance, Government of India. Through repeated discussions and collective efforts in the Empowered Committee, it was possible within a period of about a year and a half to achieve nearly 98 per cent success in the first two objectives on harmonization of sales tax structure through implementation of uniform floor rates of sales tax and discontinuation of sales-tax related incentive schemes. As a part of regular monitoring, whenever any deviation is reported from the uniform floor rates of sales tax, or from decision on incentives, the Empowered Committee takes up the matter with the concerned state and also the Government of India for necessary rectification.

The Committee of Finance Minister (in 1995 and 1998) has put forward recommendations to replace sales tax by Value Added Tax (VAT). Further the conference of Chief Minister and the Finance Minister has proposed introduction of VAT by April 1, 2002 with uniform floor rates. The Empowered Committee of State Finance Ministers on February 8, 2003 again endorsed the suggestion that all the State legislations on VAT should have a certain minimum set of common features. Most of the States came out with their respective draft legislations. Shri Jaswant Singh the then Union Finance Minister, also announced the introduction of VAT from 1st April, 2003 in his 2003-2004 budget speech made on February 28, 2003. Owing to some unavoidable circumstances, VAT could not be implemented w.e.f. April 1, 2003 and also on the revised date June 1, 2003, despite all obstacles, Haryana was the first State to implement VAT w.e.f. April 1, 2003. In rest of the States VAT Laws were at draft stage.

The Empowered Committee of the State Finance Ministers constituted by the Ministry of Finance, Government of India, on the basis of the resolution adopted in the conference of the Chief Ministers on November 16, 1999 under the Chairmanship of Dr. Asim Dasgupta came out with a White Paper on State-Level VAT, which was released on January 17, 2005 by Shri P. Chidambaram, The Finance Minister, Government of India. On this occasion the Finance Minister remarked:

“This is the first document which has been collectively prepared and put out to the people of the country by the Finance Ministers of all States.... We have formed the rainbow coalition to undertake one of the biggest tax reforms.”

This Paper consists of three parts. In Part I, justification of VAT and the background has been mentioned. In Part II, main Design of VAT as evolved on the basis of consensus among the States through repeated discussions in the Empowered Committee has been elaborated. In Part III, other related issues for effective implementation of VAT have been discussed.

The White Paper specified that registration under the VAT Act shall not be compulsory for the small dealers with gross annual turnover not exceeding ₹5 lakh. However, the Empowered Committee of State Finance Ministers has subsequently allowed the States to increase the threshold limit for the small dealers to ₹10 lakh, but the concerned State shall have to bear the revenue loss, on account of increase in the limit beyond ₹5 lakh. The VAT Acts are designed so that high value taxpayers should not be spared and on the contrary small dealers should be hassle free from compliance procedures.

The objective of all such composition schemes is not to burden small dealers by the provisions of record keeping. Therefore, such schemes will generally contain the following features:

- (i) *small amount of tax shall be payable;*
- (ii) *there shall be no requirement to calculate taxable turnover;*
- (iii) *a simple return form to cover longer return form shall be sufficient.*

All sales or purchases of goods made within the State except the exempted goods would be subjected to VAT as a consumption tax.

In his speech introducing Union Budget 2005-06, the Hon'ble Finance Minister said, "In a remarkable display of the spirit of cooperative federalism, the States are poised to undertake the most important tax reform ever attempted in this country. All States have agreed to introduce the Value Added Tax (VAT) with effect from April 1, 2005. VAT is a modern, simple and transparent tax system that will replace the existing sales tax and eliminate the cascading effect of sales tax.

In the medium to long term, it is my goal that the entire production/distribution chain should be covered by a national VAT, or even better, a goods and services tax, encompassing both the Centre and the States.

The Empowered Committee of the State Finance Ministers, with the solid support of the Chief Ministers, has laboured through the last seven years to arrive at a framework acceptable to all States. The Central Government has promised its full support and has also agreed to compensate the States, according to an agreed formula, in the event of any revenue loss. I take this opportunity to pay tribute to the Empowered Committee, and wish the States success on the introduction and implementation of VAT".

Methods of Computation

VAT can be computed by using any of the three methods detailed below:

1. **The Subtraction method:** Under this method the tax rate is applied to the difference between the value of output and the cost of input;
2. **The Addition method:** Under this method value added is computed by adding all the payments that are payable to the factors of production (viz., wages, salaries, interest payments, profit etc.);
3. **Tax Credit method:** Under this method, it entails set-off of the tax paid on inputs from tax collected on sales. Indian States opted for tax credit method, which is similar to CENVAT.

Procedure

The VAT is based on the value addition to the goods and the related VAT liability of the dealer is calculated by deducting input tax credit from tax collected on sales during the payment period. This input tax credit is given for both manufacturers and traders for purchase of input/supplies meant for both sales within the State as well as to the other States irrespective of their date of utilization or sale. If the tax credit exceeds the tax payable on sales in a month, the excess credit will be carried over to the end of the next financial year. If there is any excess unadjusted input tax credit at the end of the second year then the same will be eligible for refund. For all exports made out of the country, tax paid within the State will be refunded in full. Tax paid on inputs procured from other States through inter-State sale and stock transfer shall not be eligible for credit.

The existing Sales Tax Acts in all states will give place to the State VAT Act. Accordingly the rules,

schedules and Forms under the erstwhile Acts will be abolished. However, Central Sales Tax will continue to govern inter-State Sales and Exports.

Rates of Tax

As contrasted to the multiplicity of rates under the existing regime, VAT will have 4 broad rates-

- 0% (Exempted) for unprocessed agricultural goods, and goods of social importance),
- 1% for precious and semiprecious metals,
- 4% for inputs used for manufacturing and on declared goods, capital goods and other essential items,
- 20% for demerit/luxury goods and
- the rest of the commodities will be taxed at a Revenue Neutral Rate of 12.5%.

LESSON ROUND UP

- Taxes are classified as Direct Taxes and Indirect Taxes, Direct taxes are paid by taxpayer directly from his income/wealth etc. Whereas indirect taxes are paid by taxpayer indirectly i.e. he pays the same at the time of purchasing goods and commodities, paying for services etc.
- The Constitution of India is the supreme law. All other laws emanate from the Constitution. Articles 245 to 255 provide for the distribution of taxation powers between the Union and the States.
- The major form of levy of indirect taxes is in the nature of Excise Duty, Customs Duty, Service Tax, Central Sales Tax and Value Added Tax.
- The Central Excise duty is administered by the Central Government under the authority of Entry 84 of the Union List (List I) under Seventh Schedule read with Article 246 of the Constitution of India.
- The levy of custom duty is specified in the Customs Act, 1962 whereas the detailed classification of goods is given in the Customs Tariff Act, 1975.
- A negative list of services implies that there is, a list of services which are not be subject to service tax. Service tax will not be chargeable on the services mentioned in the negative list and which are exempted by issue of notification.
- As regards sales-tax both the Union and the States have the power to levy sales-tax.
- Under entry 92A of the Union list, the Union Government has power to levy *taxes on the sale or purchase of goods other than newspapers where such sale or purchase takes place in the course of inter-State trade or commerce.*
- Under Entry 54 of the States List the States have power to *levy tax on sale or purchase of goods other than newspapers subject to the provisions of Entry 92A of the Union List.*
- The Value Added Tax (VAT) in India is a state level multi-point tax on value addition which is collected at different stages of sale with a provision for set-off for tax paid at the previous stage i.e., tax paid on inputs. It is to be levied as a proportion of the value added (i.e. sales minus purchase) which equivalent is to wages plus interest, other costs and profits.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation)

1. What are the essential principles of Taxation ?
2. What provisions have been made in the Constitution of India in relation to authorisation of levy and collection of Central Excise duty ?
3. Who is empowered to levy and collect the duties of Excise, Customs and Sales Tax as per the provisions of Constitution of India ?
4. What is the importance of Indirect Taxes in the total tax revenues of the Government of India ?
5. In what manner the duty of Customs, Excise and Sales Tax an important source of Indirect Tax ?
6. What is Provisional Collection of Taxes Act, 1931? What is its significance in Indirect taxes?

SUGGESTED READING:

- (1) Constitution of India — *Durga Das Basu*
- (3) Budget Documents — *Govt. of India Publication*
- (4) Economic Survey — *Govt. of India Publication.*

Lesson 5

Central Excise Law

LESSON OUTLINE

This lesson is divided into the following parts covering the whole Central Excise Law:

- I. Basis of Chargeability of Excisable Goods
- II. Classification of Goods
- III. Valuation of Excisable Goods
- IV. Registration, Assessment, Payment, Clearance and Exemption of Duties
- V. CENVAT Credit Rules, 2004
- VI. Export Benefits and Procedures
- VII. Recovery and Refunds of Duties under Central Excise
- VIII Small Scale Units – Applicable Laws for Excise Duty Concessions
- IX Offences, Search & Seizer and Appellate Procedures.

LEARNING OBJECTIVES

Excise duty is levied in accordance with the provisions of Central Excise Act, 1944. It is the basic Act which lays down the law relating to levy and collection of Central Excise duty. The legislation provides for the parameters for levy of duty like when the duty is to be charged, how the goods are to be valued for the purpose of duty, how the duty would be regulated and administered. Central Excise duty is an indirect tax levied on those goods which are manufactured in India and are meant for home consumption. The taxable event is 'manufacture' and the liability of central excise duty arises as soon as the goods are manufactured. It is a tax on manufacturing, which is paid by a manufacturer, who passes its incidence on to the customers.

After completion of this lesson students will

- have the understanding of Central Excise Law
- be familiar with the practical application of Central Excise Law
- be familiar with the CENVAT Credit provisions, procedural aspect, appellate provisions, exemption provisions of Central Excise Law
- be able to do the valuation of excisable goods.

The Central Excise law is administered by the CBEC through its field offices. For this purpose, there are in all 10 zones and each zone is headed by Chief Commissioner of Central Excise. There are 61 Commissionerates in these zones headed by Commissioner of Central Excise. Under these Commissionerates there are Divisions and Ranges headed by Deputy/Assistant Commissioners of Central Excise and Superintendents of Central Excise respectively.

CENTRAL EXCISE LAW

PART I: BASIS OF CHARGEABILITY OF EXCISABLE GOODS

After completion of this part, students will be well-acquaint with the basic governing principles of excise law such as;

- Basis of levy of excise duty
- What is the taxable event for chargeability of excise duty
- Who is liable to pay the excise duty
- Relevant case studies

BASIS OF LEVY OF EXCISE DUTIES

The power to levy and collect excise duties has been conferred on the Union Government by virtue of Article 246 of the Constitution of India.

Entry 84 of the Union List empowers the Central Government to levy duty of Excise on Tobacco and other goods manufactured or produced in India excluding alcoholic liquors for human consumption, opium, Indian hemp and other narcotic drugs and narcotics but including medicinal and toilet preparations containing alcohol or opium, Indian hemp or other narcotic drugs.

It means that only the goods, which are produced or manufactured in India, can become liable to excise duties.

Thus, the statutory authority to levy duty of excise has been conferred by the Constitution on the Union Government.

CHARGEABILITY OF EXCISE DUTY

Section 3 of Central Excise Act, 1944 empowers the Central Government to levy duty of excise on excisable goods produced or manufactured in India. Section 3 of the Act is the charging section, and derives its authority from entry 84 of the Union List (List I), Seventh Schedule read with Article 246 of the constitution of India. It also specifies the conditions under which Excise Duty is leviable on all excisable goods which are manufactured or produced in India.

Duties specified in First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985 to be levied under Section 3.

Section 3 the charging section have identified four basic conditions for taxability of goods. For anything to be liable to excise duties, it must fulfill all the following conditions:

- (a) It must be “goods”;
- (b) It must be “excisable goods”;
- (c) It must be either produced or manufactured
- (d) Such manufacture or production must be in India.

Section 3(1) of Central Excise Act, 1944 prescribes the following:

- *The basic duty called CENVAT is levied and collected on all excisable goods manufactured or produced in India.*

- *Levy and collection will be as per the rates specified in the First Schedule to CETA*
- *A duty called SED (Special Excise duty) is also levied and collected on excisable goods specified in the second schedule.*
- *Such levy and collection of SED will be as per the rates in the Second Schedule.*
- *SED is in addition to CENVAT.*
- *Goods manufactured in SEZ units are excluded from levy as the SEZ is considered a foreign territory.*
- *Even govt. is subject to levy for manufacture of excisable goods. [Section 3(1A)]*
- *In case of goods cleared by an EOU, for domestic tariff area, a duty equivalent to import duty is payable.*

Through Section 3, the Union legislature has thus, done the following:

- (a) Created the duty;
- (b) Given a name to the duty;
- (c) Conferred the authority to levy and collect the duty;
- (d) Defined the scope of the duty;
- (e) Provided for specifications of the rates at which the duty shall be charged.

TAXABLE EVENT

While the duty no doubt is on goods as such, still, goods themselves cannot pay duty. This takes us to the next concept of “**TAXABLE EVENT**”. For every tax, whether direct or indirect, there is a “taxable event”. That is the event or situation which gives rise to the liability to the tax in question being created. In regard to import duties, it is the act of import which creates the liability. In as much as excise duties are duties on goods produced/manufactured, the taxable event is production or manufacture. Since, as noted, goods cannot pay duty, the *person* who created the taxable event is the person who must discharge the liability which he has created, which would mean that he should be the person to pay the duty. Since the taxable event is production/manufacture, by implication, the person who is to pay the excise duty is the producer or the manufacturer. Hence, the last of the basic concepts which will determine the duty liability in Central Excise is “manufacturer/ producer”.

The four basic concepts in Central Excise having thus been identified, we may now examine the scope and meaning of each such concept and the controversies pertaining to it as well.

THE CONCEPT OF “GOODS”

Central Excise duty is levied on goods which are manufactured or produced in India. The understanding of term goods is of wide importance in determining the liveability of Excise Duty. The Act does not define the term "goods". However, with effect from 10.05.2008 the meaning of goods has been clarified by inserting an explanation to section 2(d) wherein excisable goods are defined.

Accordingly, “Goods” includes any article material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable.

The scope of the term Goods can also be derived from various definitions available elsewhere:

- (a) *Article 366(12) of the Indian Constitution* contains an inclusive definition which says that “goods” includes all materials commodities and articles. Being an inclusive definition, this does not help much in pin-pointing the meaning of term as such.

- (b) *Section 2(22) of the Customs Act, 1962* defines "goods" to include vessels, aircraft and vehicles; stores; baggage; currency and negotiable instruments and "any other kind of moveable property". This definition framed specifically for Customs purposes may not be of much utility as determining the scope of "goods" indigenously manufactured, for purposes of excise taxation.
- (c) Section 2(7) of the Sale of Goods Act, 1930 defines "goods" as to mean "every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale". While the second part of this definition is of an inclusive nature, the first part is quite specific.

According to this definition, every kind of movable property other than actionable claims constitutes 'goods'.

The inserted explanation is more or less based on the landmark judgment of the Supreme Court in the case of *Delhi Cloth and General Mills (supra)*, where it is held that an 'an article can be called "goods" if it is known to the market as such and can ordinarily come to the market for being bought and sold. Actual sale of the article is not important but it must be capable of being bought and sold'.

Thus, movability and marketability are the two constituents of goods which require close study.

MOVABILITY & MARKETABILITY

Movability is an inherent and inseparable feature of goods whereas marketability is an integral part of excisable goods. Because excise levy is on the event of manufacture, it presupposes that only movable goods are manufactured; roads, dams, buildings etc. are not manufactured. So, anything that comes into existence as immovable cannot be subjected to levy under excise as immovables cannot be manufactured; they can only be constructed, built and so on.

Hence, the entire discussion on goods revolves around the two concepts movability and marketability.

Since excisability can be attached to manufactured goods only when they are movable and marketable, there is a lot of judicial enquiry into them. The issue of marketability is more or less well set at rest but the hitch of movability seems to be still pricking. Particularly, whether plant and machinery assembled at site and embedded in the earth are (movable) goods or not is a major area that is to be addressed fully and satisfactorily. A close examination of these two concepts movability and marketability is necessary to understand excisability.

1. Movability

Goods are necessarily movable. There are moments of confusion which have drawn the attention of the judiciary as to what constitutes movability to attract excise levy.

The word movable means capable of being moved or shifted from one place to another place. The word goods applies to those which can be brought to market for being bought and sold. It implies that the goods are movable. In *CIT v. N.C. Budharaja and Co.* (1993) S.C. it was held that the words manufacture/production are associated with movabilities - a dam or road is constructed - not manufactured or produced'. However, when an item emerges as a result of erection, installation or assembly attached to earth, it created controversy.

Things attached to the earth are generally not moveable goods. Attached to the earth has been defined under Transfer of Property Act as

- (a) rooted in the earth, as in the case of trees and shrubs

- (b) embedded in earth, as in the case of walls or buildings; or
- (c) attached to what is so embedded for the permanent beneficial enjoyment of that to which it is attached.

Movability of Goods Assembled at Site/Embedded In Earth/Site Related Activity: Whether a particular thing attached to the earth is movable or immovable depends on the mode of annexation or attachment. If a plant or machinery is fixed on the land permanently, then it is immovable property. If it is fixed on a temporary basis, it is *movable*. *Only movable property is subject to excise duty.*

The following points explain movability:

1. Movability cannot be determined on the basis of description or on the basis of their mention in CETA. It is to be judged from its state and condition at the time of removal. If an item is movable at the time of manufacture and removal, it is enough to levy duty though later on it is attached to earth permanently (*TISCO Ltd.*)
2. If the goods can be shifted from one place to another place in the same position for use, they are movable. If they have to be dismantled for erection at some other place, they are immovable and as such they are not excisable. [*Municipal Corporation of Greater Bombay, SC.*]
3. If a structure is developed on earth then it is not movable. In *MITTAL ENGINEERING WORKS* case, the Supreme Court maintained that Mono vertical crystallisers [used in sugar factories for exhaustion of molasses from sugar] were assembled, erected and attached to the earth on a permanent basis. Held that the plant came into existence as immovable property and hence not excisable.
4. If the erection of machinery is only for operational efficiency and or safety or to avoid wobbling, the machinery is movable goods (*SIRPUR PAPER MILLS Ltd. 1997, S.C.*)
5. TURBO ALTERNATOR erected on a platform to generate electricity on a permanent basis was held as immovable. Hence not excisable. As it cannot be removed as such without dismantling, it cannot be said to be goods for the purpose of levy. [*Triveni Engg and Industries Ltd v. CCE 2000 S.C.*]
6. Whether a given item is movable or not is a question of fact to be decided on case to case basis.

The expression "moveable property" has also defined in Section 3(36) of the General Clauses Act, 1897 as under:

"Section 3(36): "movable property" shall mean property of every description, except immovable property."

Example:

Solidmec marketing company was engaged in setting up of Asphalt Batch Mix, Drum Mix/Hot Mix Plant by assembling and installing the parts and components manufactured by the manufacturing units of the group. The dimensions of the plant were substantial comprising three main components namely, 4 bin feeder, the conveyor and dryer unit which were separately embedded 1.5 feet deep. Whether the assembled plant is excisable good or not ?

Solution: It is held by the Supreme Court in the case **Solid & Correct Engineering Works (S.C) 2010** that the plant is a movable property, for

- (i) It is not intended to be permanent at a given place.
- (ii) The plant can be moved **and is indeed moved after the road construction or repair project** for which its set up is completed.

2. Marketability

An item of excisability must necessarily pass the test of marketability. Marketability means saleability or suitability for sale. The test of marketability is also known as vendibility test.

Marketability is the acid test of excisable goods. Any event of manufacture resulting in goods must necessarily pass the test of marketability. It must be remembered that all goods are naturally movable but may not be marketable. Only those excisable goods manufactured are subject to levy of excise which are marketable. Since the prime purpose of manufacture is to sell, it is unthinkable of the manufacture of non saleable goods under the excise law. Right from DCM case, the apex court has been consistently holding that goods to be excisable, must be marketable.

Since marketability means saleability or suitability for sale, goods fit for sale, use or consumption are marketable goods. Goods without commercial utility or economic value cannot be considered marketable goods.

Important Points regarding Marketability

- Marketability is saleability and not necessarily actual sale.
- Even actual sale makes the goods marketable as per the amendment in 2008.
- Marketability is not dependent on nature or description of goods. Even intermediate goods, defective goods, waste/ scrap are marketable if they are saleable in their condition.
- Even goods of short shelf life are marketable if they are sold during their short life.
- Goods not identifiable in the market as goods are not marketable.
- Even a single buyer is enough to call the goods marketable..
- Marketability presupposes movability. Goods which are not movable are not marketable for the purpose of excise. To be marketable, goods must be capable of being brought to the market to be bought and sold.
- Marketability is a question of fact to be decided in each case.
- Goods specified In Tariff Act do not automatically qualify for marketability. It is to be proved independently that the goods are also marketable.
- When marketability is in dispute, the burden of proof lies on the department.

Conclusion

Manufacture is complete only when the goods are marketable, though they may not be actually marketed or sold. Finished goods or semi-finished goods are goods for excise purpose only when they are marketable. Even intermediate products captively consumed in production of final products, are excisable goods if they are identifiable as goods and are marketable.

Example:

Star laminates Ltd. manufactured laminate sheets. In the process of manufacture a solution named "Rasol" whose life was short and which was also not marketable came into being. The Assistant Commissioner of Excise issued notice to the assessee demanding duty on Rasol for the reasons that Rasol is included in the tariff schedule and dutiable. The assessee has filed objection to the demand by contending that no duty can be demanded only because of inclusion of a commodity in the tariff schedule, if it is not marketable or capable of being marketed. Decide the issue with the help of decided case law, if any.

Solution: From the facts given above, we can draw the following points for consideration

- Assessee refuse the charge on the ground that mere specification in Tariff Act is not enough.
- To impose duty the goods must also be marketable.
- The solution called Rasol is of short life and NOT marketable.
- The department demands duty on the ground that the item is in the Tariff Act and hence dutiable.
- Earlier in Moti Laminates case and also subsequently in Ion Exchange (I) Ltd case, the Supreme Court held that marketability is an independent test. All tariff items are not necessarily marketable. Only those tariff items which are marketable attract duty.

Hence, in the instant case, the solution 'Rasol' is not dutiable because it is not marketable.

Case Studies on Marketability

(1) Marketability is not dependent on actual sale. It is enough if the goods are capable of being sold. Simply because there is a statutory prohibition that free samples shall not be sold, the goods cannot be treated as nonmarketable. Therefore, free distribution of physicians samples are marketable in case of **Medley Pharmaceuticals Ltd. 2011(S.C.)**

(2) Usha Rectifier Corp. (I) Ltd. v. CCEx., New Delhi 2011 (263) E.L.T. 655 (S.C.)

Facts: The company is a manufacturer of electronic transformers, semiconductor devices and other electrical and electronics equipments. During the course of such manufacture, the company also manufactured machinery in the nature of testing equipments to test their final products.

Issue: Whether assembling of testing equipment for testing the products of the company are subject to duty.

Decision: Yes. The contention of the company that the testing equipment was developed internally to avoid imports and forex outflow, proves that the goods are marketable. Hence the capital goods captively used are excisable. Duty is payable as the captive consumption constitutes removal.

3. Bata India Ltd. v. CCE 2010 (252) ELT 492 (SC)

Facts: During the manufacture of foot wear the assessee manufactures an excisable product called double textured fabric which emerges as a distinct product with specific properties and character which is used in considerable quantities for making rain-coats, holdalls, hand bags etc. The department issued show cause notices to the assessee.

Issue: Whether unvulcanised sandwiched fabric assembly produced in the Assessee's factory and captively consumed can be termed as "goods" and can be classified as "rubberized cotton fabrics"

Decision: Revenue did not succeed in establishing that the product in question was either marketed or was capable of being marketed, thus held that without proof of marketability, the intermediate product would not be goods under excise for levy.

4. Nicholas Piramal India Ltd. v. CCEx., Mumbai 2010 (260) E.L.T. 338 (S.C.)

Issue: Whether vitamin A acetate crude and vitamin A palmitate or crude vitamin A captively consumed to manufacture animal feed supplement and not sold are subject to levy if they satisfy the test of manufacture and marketability.

Held: Actual sale is not necessary. Saleability of a product is enough. Even short shelf life goods can be

marketable if they are capable of being bought and sold during their short life. The fact that the assessee had to buy same intermediate products from the market if not captively consumed shows marketability of goods. As per the facts available, the products are capable of being sold and known in the market. Hence the above products are liable to duty.

Short shelf life is different from no shelf life. The product in the instant case has a shelf life of 2 to 3 days. The Supreme Court held that shelf life of 2 to 3 days is sufficient for product to be commercially marketed.

RELATED CONCEPTS OF GOODS UNDER CENTRAL EXCISE

(a) Goods v. Excisable Goods: As cleared already, goods mean those items which are movable and marketable at the stage of their production/ manufacture. Excisable goods means those goods specified in Central Excise Tariff Act and subject to duty. Certain goods specified in the Schedule I to Central Excise Tariff Act carry NIL rates. Those having nil rate are leivable goods and those having some rate of duty are also leivable goods. Even the nil rated goods, are excisable goods. Exempted goods, needless to say, are also excisable goods. So, excisability of an item is not based on its dutiability, rather it is based on its placement in the Schedule to the Tariff. Again mere mention in Tariff is not enough to make it excisable. The manufactured goods having marketability become excisable.

(b) Leivable Goods v. Dutiable Goods: All excisable goods having some rate of duty are leivable goods. But leviability does not mean dutiability. When leivable goods are fully exempted from duty by a notification under Section 5A, they become non-dutiable goods. Dutiable goods are those on which duty is finally payable. Hence, all dutiable goods are leivable goods and all leivable goods are not necessarily dutiable.

(c) Exempted Goods v. Nil Rated Goods: Exempted goods means goods exempted by a notification under Section 5A of the Central Excise Act. But goods removed under bond are not exempted goods. Exempted goods are basically leivable goods. Fully exempted goods may become dutiable at the time of removal if the exemption is withdrawn by that time. For example, in Wallace Floor Mills Co. Ltd. v. CCE 1989 (44) ELT 598, when the goods were manufactured and packed they were fully exempt from duty. At the time of removal of goods from factory, the exemption was withdrawn. The Supreme Court held that the goods are dutiable and hence duty is payable.

The above land mark ruling established the point that dutiability is finally determined at the time of removal and not at the time of manufacture though the taxable event is manufacture. In other words, rate of duty prevailing at the time of removal and not at the time of manufacture, is relevant.

But same is not the case with NIL rated goods. When goods carry nil rate at the time of manufacture, they continue to be nil and no duty is payable on them unless there is a subsequent change in the tariff rate. Subsequent change may have immediate effect by virtue of Provisional Collection of Taxes Act 1931.

Moreover, if there is a subsequent change in classification of goods in question after manufacture but before removal, the latest classification number applicable at the time of removal will be relevant, which may turn out to be favourable or unfavourable to the assessee.

(d) Non-dutiable Goods v. Non-excisable Goods: Fully exempted goods are non-dutiable goods and non-excisable goods are non-leivable goods. In case of fully exempted goods, the effective rate of duty is Zero (Tariff rate minus exempted rate is effective rate). The fate of dutiability of exempted goods is decided at the time of their removal. The nil rated goods' fate is predetermined at the time of manufacture itself. They normally continue to enjoy the privilege of being nil until and unless they are brought under some other classification carrying some rate of duty at the time of removal or a fresh levy was made after manufacture but before removal.

Non duty paid goods are different from non dutiable goods. They are goods removed clandestinely (secretly) without invoice to evade duty.

(e) Non excisable goods v. Nil rated goods: Non-excisable goods are those goods not in the Tariff Act. Nil rated goods are CETA specified goods carrying nil rate or they can be called as goods chargeable to nil rate of duty. While the non excisable goods cannot be made excisable with retrospective effect, they continue to enjoy the status of non excisability even at the time of removal. It means goods non-excisable at the time of manufacture will continue to be non-excisable till end and any change in their status after manufacture and before removal will not affect them.

Nil rated goods, on the other hand, are excisable goods. Goods chargeable to nil rate may become dutiable at the time of removal if there is change in the tariff rate after manufacture but before removal. This may happen either due to change in classification number or change in tariff rate. Such changes are normally brought forth through Finance Act or by using emergency power under Section 3 of Central Excise Tariff Act, 1985.

THE CONCEPT OF 'EXCISABLE GOODS'

Once it is established that something falls within the ambit of the term "goods" then the issue to be decided is whether it is also "excisable goods".

The term "excisable goods" has been defined in Section 2(d) of the Central Excise Act 1944. It says that the term "excisable goods" means

"Goods specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act 1985 as being subject to a duty of excise and includes salt".

Explanation: "goods" includes any article material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable.

The definition in Section 2(d) is specific to the effect that it is only goods spelt out in the Tariff as being subject to duty that can be considered to be excisable goods. This would mean that it is only till the stage when the duty liability is not discharged by actual payment, that the goods can be called 'excisable goods'.

Once the duty is paid or the goods have been subjected to duty, they are not excisable goods. In sum, excisability attaches itself to the goods only till the point of payment of duty. Duties paid goods are not excisable goods.

In fact, this criterion is more specifically brought out in the Customs Act, 1962. While defining the corresponding tax liability on goods viz., "imported goods", Section 2(25) of the enactment defines imported goods as those which are brought into India from a place outside India, and makes it very clear that the term "imported goods" does not include goods which have been cleared through Customs for home consumption. Goods coming from abroad and cleared by Customs may be foreign goods but they are not imported goods (for purposes of Customs Law). Similarly, goods manufactured in India, once they are cleared from the factory on payment of duty may continue to be manufactured goods, but they are not excisable goods (for purposes of Excise Law).

The following points are relevant for excisable goods:

- *Nil duty paid goods are also excisable goods, though duty is not paid, they do not lose their excisability. The mere fact that rate of duty on an article is NIL by reason of an exemption notification would not make it non-excisable goods. [UOI v. Nandi Printers, 2001 S.C. 127 ELT 645].*

- Only those goods mentioned in the Central Excise Tariff Act, 1985 are excisable but they must be movable and also marketable for levy.
- Goods from scrap waste or intermediate products for captive consumption are also excisable goods if they are mentioned in Central Excise Tariff Act, 1985.
- Duty paid goods cease to be excisable goods as they have already been subjected to excise duty.

Conclusion

A manufactured item should necessarily find a place in Central Excise Tariff Act, 1985; otherwise, it is not excisable.

CONCEPT OF MANUFACTURE

Once it is established that what comes up for assessment is actually 'goods', and furthermore, is 'excisable goods', it is still to be established that there has been a manufacture thereof. This is because Section 3 of the Act authorizes levy and collection of excise duties only on excisable goods produced or manufactured in India. This takes us to the third concept viz., "manufacture".

This concept has not been defined in specific terms by the Act, and this omission, (deliberate or otherwise) has given rise to a spate of disputes. Before these are taken up for examination, the statutory definition under Section 2(f) may be examined.

Section 2(f) of the Act provides an inclusive definition of the term by saying that manufacture includes any process

- incidental or ancillary to the completion of a manufactured product
- which is specified in relation to any goods in the Section or Chapter Notes of the First Schedule to the Central Excise Tariff Act 1985 as amounting to manufacture or
- which in relation to goods specified in the third schedule to Central Excise Act 1944 involves packing or repacking of such goods in a unit container or labeling or relabelling of containers including declaration or alteration of retail sale price on it or adoption of any other treatment on the goods to render the product marketable to the consumer;

and the word "manufacturer" shall be construed accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods, but also any person who engages in their production or manufacture on his own account;

Thus, the definition of manufacture u/s 2(f) is in three parts, namely:

- (i) Incidental or ancillary process to the completion of a manufactured product.
- (ii) Deemed manufacturing processes specified in Central Excise Tariff Act, 1985.
- (iii) In relation to specific goods, processes are specified under Schedule III of Central Excise Act, 1944.

In fact, for the Schedule III items, valuation scheme based on retail sale price (under Section 4A) is applicable.

The phrase "incidental or ancillary to the completion of a manufactured product" deserves to be examined. Manufacture of any product is through a series of manufacturing processes taking place in sequence. At a

particular stage, after the necessary processes are completed, the product emerging may be functional. Nevertheless, a few more processes may be necessary to render the product saleable. As noted earlier, it is saleability which is the crucial criterion for deciding excisability. Hence, the processes which take place to render the product which is already functional to become one which is also saleable, are those which can be considered as “incidental or ancillary to the completion” of the manufactured product.

Example

To illustrate, A piece of steel furniture, say a cup board, while being manufactured in a factory, emerges at a stage when it can function as a cup board, though it is still to be given spray painting etc. In such a situation, painting is a process ancillary to complete the cup board as a manufactured product capable of being sold. In this case Excise duty can be charged only after the painting process is completed.

CASE STUDIES RELATING TO MANUFACTURE

In the absence of a specific definition of “manufacture” in the Act, resort has to be made to pronouncements made in various judicial forums where this concept came up for examination. Important pronouncements of various courts in this regard are as below:

(1) *Flex Engineering Ltd. v. Commissioner of Central Excise, U.P. 2012 (276) E.L.T. 153 (S.C.)*

Facts: The assessee is engaged in the manufacture of various types of packaging machines known as F & S machines. The machines are made on order according to the specification of individual customers. The machines are required to be tested before dispatch, by the customer; the assessee makes entry in Daily Stock Account declaring the machine as manufactured and ready for clearance only after the customer confirms it.

Issue: *One of the issues in the above case was whether manufacture is complete before testing and acceptance by customer or manufacture is complete before testing itself.*

The department opined that testing takes place only after manufacturing of final product. Assessee's contention was that the manufacturing process was complete only after testing

Decision: The taxable event of manufacture is complete only when the goods manufactured are marketable. In the instant case the machines become marketable only after they are tested and accepted by customer. Hence no manufacture took place before testing.

(2) *Union of India v. Delhi Cloth and General Mills and others (ELT - 1977 - J. 199).*

This is a landmark judgment of the Supreme Court which settled for all purposes the scope of the concept “manufacture” in Central Excise. The facts in brief were that the parties who were manufacturers of Vanaspati purchased groundnut and Til oil from the open market. The oils thus purchased were subjected to different processes to convert them into Vanaspati. While they were no doubt paying excise duty on Vanaspati, the department contended that when the basic oils were being subjected to a series of processes, they emerged at a particular stage as a product which can be construed as “Vegetable Non-Essential Oil” (VNE), which would attract duty under a separate Tariff Item. In other words, in the department's view, there was “manufacture” of V.N.E. Oil attracting excisability, before its further conversion into Vanaspati, attracting excisability once again.

A great deal of evidence was let in by either side, which was elaborately examined by the learned Bench. It reduced the issue to the simple one whether mere processing itself can be construed to be manufactured. On this, they cited a passage quoted in the Permanent Edition of “Words and Phrases” Volume-26 from an

American judgement. The citation which has assumed tremendous import in all disputes pertaining to "manufacture" in Central Excise since then, (being frequently cited by either side to disputes) runs thus:

"manufacture implies a change but every change is not manufacture; and yet every change of an article is the result of treatment labour and manipulation. But something more is necessary and there must be a transformation; a new and different article must emerge having a distinctive name character or use".

This succinctly explains what constitutes manufacture. Manufacture implies several processes, and in each of them, by working upon what one starts with, changes are no doubt introduced. Still, such changes alone would not by themselves tantamount to manufacture. For the changes to be considered as manufacture, what results after the change should have different name, different character or different use, as against what one started with.

On this reasoning, the Supreme Court held in the D.C.M, case that mere processing of the basic oils did not tantamount to manufacture of VNE Oils, since on the basis of detailed examination of evidence, it was held that for VNE Oil popularly marketed as refined oil, the essential ingredient was that they were deodorised. On the contrary, in the cases before them, though substantial processes of purification of the basic oils had taken place, still they were not deodorised, before being converted into Vanaspati. Hence, the learned judges held that there had been no transformation bringing in new name, character or use, and hence there was no manufacture as such.

PRODUCTION, MANUFACTURE AND PROCESS DISTINGUISHED

Under excise, the taxable event is manufacture or production. Hence, examination of these two terms manufacture and production is useful.

Production is a natural process by which a product is brought into existence. E.g. Production of tobacco, iron ore, jute, flowers etc. Manufacture, on the other hand involves some artificial process which adds some more utility to the product, e.g. Tobacco is produced and cigarettes are manufactured, similarly, sugar cane is produced and sugar is manufactured. Thus, we can conclude that *every manufacture is production and every production is not manufacture*. The Supreme Court in *CIT v. N.C. Budharaja & Co. AIR (1993) S.C. 2529* held that the word production has wider connotation than 'the word manufacture'. Every manufacture can be characterised as production but every production need not amount to manufacture.'

But it may be noted that under excise, manufacture is more relevant than production since many items of production are either not excisable or exempted from duty.

What is process?

The term process has not been defined in the Act. The dictionary meaning of process is a continuous and regular action or succession of actions taking place or carried on in a definite manner and leading to accomplishment of some results. In the context of excise, a process is an operation or activity which may or may not result in production/manufacture. Usually, there are series of operations which bring into existence an item with a distinct name, character or use. For example, series of processes culminate in the production of rice; viz., ploughing, watering, sowing seeds, transplantation, weeding and harvesting. With the final process of harvesting, paddy is produced and rice, from paddy. *Similarly, cotton is produced by some natural process and cloth is manufactured by artificial processes such as ginning, pressing, threading and so on. In both production and manufacture, certain processes are involved.*

For excise purpose, mere process is not enough to call it manufacture/production. Such process/processes should bring into existence an excisable entity preferably with a distinct name, character or use. For instance, a log of wood is cut into pieces. Cutting is a process, but not manufacture. Furniture is made out of

wood. The process is manufacture as it is a distinct excisable item. Hence, we can conclude that every manufacture/production is a process and not necessarily vice versa.

Case Laws relating to Production or Manufacture

1. In Empire Industries v. U.O.I. 1985 (20) ELT 179 S.C. the honourable court observed 'Processing' is different from manufacturing and mere change or processing does not mean manufacture. Any process creating something else having distinctive name, character or use would be manufacture. In this case, the apex court held that processing grey fabrics by bleaching, dyeing, and printing of fabric will amount to manufacture.

2. In CCE v. Rajasthan State Chemical Works 1991 (55) ELT 444 S.C. The term process has come to be examined again. The apex court observed:

“Manufacture involves series of processes. Process in manufacture or in relation to manufacture implies not only the production but the various stages through which the raw material is subjected to change by different operations. Each step towards production would be a process in relation to the manufacture. A process is a manufacture when it brings out a complete transformation so as to bring new commercially different article or commodity."

The court in the instant case held that to be a process, no physical/chemical change is necessary. Even material handling is a process of manufacture.

3. Decorative Laminates v. CCE (1996) S.C: A further process can be a manufacture even if the final product and the input fall under the same tariff.

Duty paid commercial plywood was reprocessed to produce slip proof commercial plywood. The process is an application of PF resin on duty paid plywood under 100% heat and, pressure and coating it with wire mesh to make it slip proof commercial plywood. This product is used in body building or flooring. In fact both input and the final product fall under the same classification No. [44.08]. Held that slip proof commercial plywood is a manufacture resulting in a distinct product. The court based its decision in Laminated Packagings (P) Ltd.

Earlier, the same court in Laminated Packaging (P) Ltd. 1990 held that laminated kraft paper with polyethelene amounts to manufacture as kraft paper and laminated kraft paper are two distinct products.

4. CCE v. Kapri International (P) Ltd. 2002 (142) ELT (S.C.)

Issues: (i) Whether cutting cotton fabrics from running length into small pieces such as bed sheets, table cloths, napkins and pillow covers amounts to manufacture ?

(ii) Whether duty paid raw material (cotton fabrics in this case) and final products (pillow covers, napkins etc.) falling under same tariff item can be subjected to multiple levy.

Decision: The Honourable Supreme Court held that by cutting the cotton fabrics from running length into small pieces and giving them a definite required shape to form new articles like, bed sheets, bed spreads, table clothes etc, the respondent has produced a new commodity which has a definite commercial identity in the market. [Hence, it amounts to manufacture.]

On the question of dutiability the court observed that the mere fact that the material from which the new goods are manufactured, has suffered duty under a particular tariff item, that does not exclude the finished product from being eligible to fresh duty if the tariff Act provides for it. In the instant case, though the cotton fabrics had suffered duty under tariff item, the Tariff Act has made bed sheets, pillow covers etc., also

dutiable under the very same tariff item, therefore the respondent is liable to pay duty on bed sheets etc. also manufactured by it.

NOTE: The SC relied on its earlier decision in Laminated Packagings (P) Ltd., 1990.

DEEMED MANUFACTURE

Processes specified in Central Excise Tariff Act, 1985 amounting to manufacture/deemed manufacture. The test of transformation was applied by Supreme Court from time to time to determine whether a process is a manufacturing process or not. But in many a case where the department lost the cases and where it felt that the process should have been chargeable, it has taken the route of deemed manufacture.

By virtue of the definition in Section 2(f), any process can be declared by the legislature as amounting to manufacture irrespective of the fact that the process is not manufacture as per transformation test. That means any process declared as manufacture does not require to pass the test of transformation laid down by supreme court in DCM case.

For instance, the Supreme Court held in Crane Betel Nut Powder Works, 2007 (S.C). Process of cutting betel nuts into small pieces and addition of essential and non essential oils, menthol, sweetening agents etc. did not result in manufacture as there is no distinct character/use.

Note 6 to chapter 21: "In relation to product of tariff item 2106 90 30, the process of adding or mixing cardamom, copra, menthol, spices, sweetening agents or any such ingredients, other than lime, katha or tobacco to betel nut in any form shall amount to 'manufacture'

Deemed manufacture –The following processes will be 'deemed to be manufacture' and duty will be payable as the process is specified in Central Excise Tariff as 'amounting to manufacture'.

Examples of deemed manufacture:

- 'Building a body or fabrication of structure on chassis shall amount to manufacture [Note 3 to Chapter 87].
- Labelling or relabelling of containers from bulk pack to retail packs or any other treatment of certain sugars including chemically pure lactose, maltose etc, making them marketable shall amount to manufacture.[chapter 17]
- Labelling or relabelling of containers and repacking from bulk pack to retail packs of pan masala shall amount to manufacture.(chapter 21)
- Labelling or relabelling of containers and repacking from bulk pack to retail packs of unmanufactured tobacco, cigars and cigarettes shall amount to manufacture.(chapter 24)
- Labelling or relabelling of containers and repacking from bulk pack to retail packs of soaps and waxes shall amount to manufacture.(chapter 34)
- Affixing brand name, labelling relabelling/ repacking of articles of apparel and clothing accessories knitted or crocheted eg. Shawls, gloves shall amount to manufacture.[chapter 61]
- Galvanisation process of articles of iron or steel shall amount to manufacture.
- Cutting / polishing of granites or marble slabs amounts to manufacture. [Note 6 to chapter No. 25]
- The process of drawing or redrawing a rod, wire or any other similar article amounts to manufacture [Note 10 to Section XV]

Chapter No. of CETA	Title of The Chapter	Process Amounting To Manufacture
Chapter 22	Beverages Spirits and Vinegar	Labelling or relabelling of containers, or packing or repacking from bulk packs to retail packs or, adoption of any other treatment to render the product marketable to the consumer.
Chapter 26	Ores	Conversion of ores into concentrate
Chapter 68, budget, 2010)		Process of cutting or sawing or sizing or polishing or any other process for converting stone blocks into slabs or tiles amount to manufacture.
Chapter 71	Gold	Process of refining of gold ore (rough) bars into tradable gold bars of high purity.
Chapter 72	Articles of Iron and Steel	Galvanization process of all articles under the chapter.
Chapter 76, budget 2010		Process of drawing or redrawing aluminium tubes and pipes amounts to manufacture.

There are 40 + processes specified in CETA which are deemed to be manufacturing processes.

Burden of Proof: when the process is not covered by CETA, or CEA, the burden of proof that the process is manufacture, is on the Department.

The processes specified in CETA have been authenticated by section 2(f) of the Central Excise Act, 1944

In **S.D. FINE CHEMICALS**, the Supreme Court upheld the validity of the list under CETA. It held that the definition of manufacture is expansive and it includes processes mentioned in CETA, even if these processes are not manufacture.

VARIOUS ASPECTS OF MANUFACTURE

(1) Assembling

- Whether assembling amounts to manufacture:** Assembly may or may not amount to manufacture. It depends on the nature of assembling activity and the resultant product.
- If a new or different article emerges as a result of assembling activity, then it is manufacture. **Eg. Assembling of various parts into a computer.**
- If different parts are put together but no new article emerges and the use of parts is same even after assembly, then there is no manufacture. Eg. Assembly of tools to make it a tool kit. In this case there is only a change in name but use of tools is same.
- Certain assembling** activity may be a deemed manufacture as per Tariff Act.

(2) Branding, Labelling, Packing, Repacking Etc.

- Branding labelling etc**, normally does not result in manufacture unless a new and different article emerges.

- (b) Such activity may be a deemed manufacture. (See labelling, relabeling etc for the consumer goods specified under Schedule III of Central Excise Act, 1944)

CASE STUDIES RELATING TO MANUFACTURE

(1) *CCE v. Osnar Chemical Pvt. Ltd. 2012 (276) E.L.T. 162 (S.C.)*

Facts: *Osnar Chemical Pvt. Ltd. (Osnar)* was engaged in the supply of Polymer Modified Bitumen (for short "PMB"). As per the agreement between Afcons Infrastructure Ltd. (Afcons) and Bitumen, the base bitumen and certain additives were to be supplied by Afcons to Osnar directly at the site, where Osnar, in its mobile polymer modification plant, was required to heat the bitumen at a temperature of 160°C with the help of burners. To this hot bitumen, 1% polymer and 0.2% additives were added under constant agitation, for improving its quality by increasing its softening point and penetration. The process of agitation was to be continued for a period of 12 to 18 hours till the mixture becomes homogenous and the required properties were met. The said bitumen in its hot agitated condition was mixed with stone aggregates which were then used for road construction. The Osnar paid duty on PMB processed at their factory in Mumbai but had not paid the same for the conversion done at their work site.

Issue: Whether the addition and mixing of polymer and additives to base bitumen results in the manufacture of a new marketable commodity and as such exigible to Excise duty. Revenue contended that such process carried out amounted to manufacture.

Held: The said process did not result in transformation of bitumen into a new product having a different identity, characteristic and use. It is well settled that ***mere improvement in quality does not amount to manufacture.***

(2) *Commissioner v. Steel Authority of India Ltd. 2012 (283) E.L.T. A112 (S.C.)*

Issue: Whether iron ore concentrate made out of iron ore after the processes of crushing, grinding, screening and washing for removing foreign materials is a distinct commercial commodity hence it is a manufactured product.

Decision: It is held that removal of foreign materials from iron ore, i.e., mining iron ore from mines and then subjecting to process of crushing, grinding, screening and washing with a view to remove foreign materials to concentrate such ores do not result in manufacture of different commercial commodity. No Central excise duty is leviable on iron ore concentrate.

(3) *GRASIM INDUSTRIES LTD. 2011 (S.C.)*

Facts: The assessee was the manufacturer of the white cement. He was using welding electrodes, steel angles, channels etc. in the process of repair and maintenance of equipment and in the process of repair some scrap were generated.

Issue: Whether scrap arising out of repairs and maintenance of machinery is dutiable under excise.

Decision: No, the generation of metal scrap or waste during the repair of machineries/parts of cement manufacturing plant does not amount to manufacture. The process of repair and maintenance of the machinery of the cement manufacturing plant, in which scrap arise, has no contribution or effect on the process of manufacturing of the cement, (the end product). The repairing activity in any possible manner cannot be called as a part of manufacturing activity in relation to production of end product. Therefore, the scrap cannot be said to be a by-product of the final product.

CONCEPT OF "MANUFACTURER"

This concept has also not been defined specifically in the statute, which however provides an inclusive definition under Section 2(f) which runs thus: "manufacture" shall be construed accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods but also any person who engages in their production or manufacture on his own account".

This inclusive definition identifies following types of parties who can be considered as manufacturers.

- (a) *Those who personally manufacture the goods in question on their own account.*
- (b) *Those who get the goods manufactured by employing hired labour.*

It is well known that sub-contracting, utilisation of facilities of ancillary units etc. are being increasingly resorted to even by major industrial units and the motivation in all such cases need not necessarily be dodging excise levies. In fact, even large public sector undertakings such as B.H.E.L. farm out production to a number of Small Scale Units, though it should not be difficult for them to manufacture those goods themselves. They do so as a matter of public policy, which is to encourage the growth of small entrepreneurs. However, there are cases where the motives may not be that honourable.

Excise department has given substantial duty concessions to the small scale sector, which reaches even to the level of no duty being charged on goods manufactured by the small scale units upto prescribed limits. Large scale manufacturers, at times, utilise this facility to avoid excise duties. It is done by supplying almost all the inputs, specifications, etc. to the small scale units, and at times even going to the extent of supervising the production by the small scale units. The goods are manufactured by the Small scale units and even the brand name of the other party (supplier of inputs, specifications etc.) affixed thereon. The goods are cleared at the concessional rate, and if the clearance is within the prescribed limits, even duty free and to that extent the ultimate price can be lesser or, in a sellers' market, the profit margin may be more. The goods are subsequently marketed by the large scale units (supplier of inputs) which stand to benefit substantially by such devices.

These matters have given rise to considerable litigation and a few important judgements in this context are as below:

- (a) ***Ujagar Prints v. U.O.I*** 1989 (39) ELT 493 (S.C.) — In this case, the S.C. has decided the core issue of valuation of goods manufactured by the job worker, while deciding that the job worker is the manufacturer and not the raw material supplier or brand owner. The Ujagar Prints were doing the process of manufacture on the materials supplied by another company. After finishing the job, the finished products were being sent back by Ujagar Prints and charging certain amount agreed upon. The charges of the processor included the processing profits. It was held that Ujagar Prints is the manufacturer and the value of goods include the processor's charges. Justice Sabya Sachin Mukharji observed:

"Duties of excise are imposed on production or manufacture of goods and are levied upon the manufacturer or the producer in accordance with the relevant rules. This is quite independent of the ownership of goods."

- (b) ***In M.M. Khambhattwala*** case, the Supreme Court followed the principle in Ujagar Prints and observed that the house ladies who manufacture Dhoop and Agarbatti at home are manufacturers as there is no supervision or control over them by the raw material supplier.

TESTS OF A MANUFACTURER

I. Relationship Test: If the relationship between the person getting the work done (through others) and the person who actually does is master-servant relationship or principal - agent relationship, then it is a case of manufacture through hired labour. If, on the other hand, the person who actually manufactures is independent, then he himself is the manufacturer. It is a case of principal to principal relationship and not of principal agent.

II. Profit Test: If the manufacturing profit is enjoyed and retained by the person who actually undertakes the process of manufacture, then he is surely independent and he is the actual manufacturer liable to pay excise duty. The profit test in fact is corollary to the test I, which further corroborates the relationship test.

Ordinarily, the following are not manufacturers —

Raw Material supplier: *If the raw material is supplied on principal to principal basis, (e.g. Bata Ltd. supplies raw material to job workers) the supplier is not manufacturer though he has a right to reject the goods.*

Brand Owner: *If the brand owner has no control over the manufacturing process/parties, he cannot be treated as manufacturer, even if he had supplied raw material and the manufacture is under his brand name [Basant Industries, Kanpur, S.C.].*

Raw material supplier is manufacturer if the manufacturer is either a dummy manufacturer or is the agent of the raw material supplier (Shree Agency).

Supplier of concentrates etc. *under franchise agreement is not a manufacturer and the bottling company is the manufacturer (Puna Bottling Co.).*

Person Supplying raw material to produce drugs though having licence to produce is not the manufacturer. Person who actually manufactures drugs is the manufacturer.

Labour contractor supplying labour is not the manufacturer for the goods manufactured by the labour supplied by him under Contract Labour (Regulation & Abolition) Act, 1970.

Conclusion: Whether the person, be it a raw material supplier or brand owner etc. is a manufacturer or not, is a question of fact. It depends upon - the type of relationship he holds with the person through whom he gets the work done (ii) the type of financial arrangement he has with such person.

He may exercise control over the quality and quantity of the production and still he may not be the manufacturer as the ultimate test is the enjoyment of profit. The burden of proof lies on that brand owner etc. to prove that he is not the manufacturer. Since the duty levied is collected from the manufacturer, it is necessary to identify the real manufacturer.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not be submitted for evaluation).

1. "Excise is a duty on goods indigenously manufactured". Explain the relevance of this statement with special reference to provisions of Section 3 of Central Excise Act, 1944.
2. What is the purpose and significance of Section 3 of the Central Excise Act, 1944?
3. What is the "subject matter" of levying of duty of Central Excise as envisaged under the Central Excise Act, 1944? Elaborate.
4. What is the concept of "goods" as envisaged under the Central Excise Act, 1944, for the purpose of levying of the duty of Excise? Explain with the help of case law, if any.

5. Is there any distinction between “Goods” and “Excisable goods”? Elaborate.
6. What is the difference between “Excisable goods” and goods which have paid the excise duty thereon?
7. Is there any difference between “Excisable goods” and “Dutiable goods”? If yes, explain clearly.
8. What is the definition of the concept of “Manufacture” in the excise law?
9. Discuss the following whether they amount to manufacture or not: 1. Assembling ; 2. Labelling/ relabeling.
10. How is the event of “Manufacture” determined for the purpose of levying of duty of Central Excise? Explain giving the latest amendments and using the case law on this matter.
11. Who is liable to pay duty of Central Excise? Explain with the help of Case Law. State the cases where a person other than a manufacturer is liable to pay duty.
12. Manufacture is independent of ownership. A person other than the owner of goods can be a manufacturer. Explain.
13. The assessee was the manufacturer of the white cement. He repaired his worn out machineries/parts of the cement manufacturing plant at its workshop such as damaged roller, shafts and coupling with the help of welding electrodes, mild steel, cutting tools, M.S. Angles, M.S. Channels, M.S. Beams, etc. In this process of repair, M.S. scrap and Iron scrap were generated. The assessee cleared this metal scrap and waste without paying any excise duty. The Department issued a show cause notice demanding duty on the said waste contending that the process of generation of scrap and waste amounted to the manufacture in terms of section 2(f) of the Central Excise Act. Examine the above with the help of the decided case if any.
14. Movability is an essential ingredient of marketability under Excise. Do you agree?

SUGGESTED READINGS

- (1) Central Excise Act, 1944 – *Bare Act*
- (2) Indirect taxes- Law & Practice – *V.S Datey, Taxmann*
- (3) Central Excise Law – *R.K Jains, Centax Publication, New Delhi*
- (4) Excise Law Times – *Centax Publication, New Delhi*

CENTRAL EXCISE LAW

PART II: CLASSIFICATION OF GOODS

At the end of this part the student will;

- Have understanding of the term “Classification”
- Have the practical knowledge of the classification process
- Able to classify the goods for the purpose of determination of duty chargeable under excise and customs
- Have understanding of the rules of interpretation

This topic is common for Central Excise law and Customs law.

INTRODUCTION

Classification means the process of determination of tariff number (classification number). Tariff Acts under Customs and Excise contain a large variety of goods. There is no single uniform rate of duty for these goods. Hence they need to be classified into different categories for easy access and convenience in ascertaining their dutiability.

In order to determine the rate of duty on a particular product, first find out the chapter heading under which the item is classifiable. Against that classification, the corresponding tariff rate has to be read with the exemption notification, if any. Thus, effective rate of duty on an item is obtained.

The Central Excise Tariff Act (CETA), 1985 and Custom Tariff Act (CTA), 1975 prescribes the rate of duty against each item and these rates are called “*Tariff Rates*”. The classification of goods is the prerequisite for determining the amount of duty to be payable.

PURPOSE OF CLASSIFICATION

Under Excise, the goods are identified by their code numbers, called as classification numbers/ tariff heading numbers. Ascertaining the classification numbers is necessary to---

- Determine excisability/ dutiability of the goods.
- Find out rate of duty applicable to such goods.
- Ascertain the duty by checking up whether any exemption is available under section 5A/ 25 as the case may be, or any new levy or increase of duty is there. Proper classification of goods ensures smooth functioning and avoids disputes.

NOTE: Dispute on classification is a significant matter and all appeals from CESTAT go directly to the Supreme Court.

CLASSIFICATION – SALIENT FEATURES

- CETA, 1985 has two schedules; schedule I has all excisable goods attracting single duty called CENVAT. Schedule II goods attract CENVAT and also SED.
- CTA, 1975 also has two schedules; Schedule I for imported goods known as “Import Tariff” and

schedule II for export goods known as "Export Tariff". The tariff schedule has rates of duties applicable to the goods.

- The classification of goods under CETA & CTA is based on Harmonised System of Nomenclature (HSN) developed by World Customs Organization of Brussels. This is a more scientific method of classification which has reduced classification disputes to a large extent.
- Classification is based on eight digit system. First two digits represent chapter number next two digits, heading number and the next two digits are sub heading numbers and including the last two digits it is called tariff heading number.
- The tariff schedule under CETA has four columns, viz (i) Tariff Items No. (ii) Description (iii) Unit (iv) Rates of duty applicable. Rate of duty in the last column may be specific i.e on quantity or % age (ad valorem). The tariff rate is subject to the relevant exemption notifications issued under section 25 of Customs Act, 1962.
- The tariff schedule under CTA, 1975 has five columns, standard rates and preferential rates are prescribed in the fourth and fifth columns respectively.
- The goods are so grouped that they are classified beginning with raw material and ending with finished goods under the same chapter.
- There are 21 sections in the tariff schedules of Excise and Customs. Each section is divided into a number of chapters and each chapter is further divided into headings and sub-headings.
- There are section notes and chapter notes to enable better understanding and proper application which have binding effect.
- There are also rules provided for interpretation in case of need. If the rules cannot be applied successfully, then the principles evolved by courts may be resorted to.
- In case of dispute over correctness of classification No, the burden of proof is on the department.

TARIFF SCHEDULE	NO. OF SECTIONS	NO. OF CHAPTERS	NO. OF COLUMNS
Central Excise	21	98 (chapters 77, 97& 98 blank)	4
Customs	21	98 (chapter 77 blank)	5 (5 th being preference rate.)

EMERGENCY POWER OF CENTRAL GOVERNMENT TO INCREASE DUTY

Any amendment to the schedule has to be effected by an amending Act or Ordinance as provided under the constitution but the Central Government has power under section 3(1) of the Central Excise Tariff Act to increase by notification the rates of duty specified in the schedule if the Central Government is satisfied that circumstances exist which render it necessary to take immediate action.

Section 3 of the Tariff Act 1985 empowers the Central Govt. to increase existing rate to the limits specified below:

- Nil rated goods can be made dutiable upto 50% of value of goods.
- Existing tariff rate of duty can be increased to twice the rate of duty specified in respect of such goods in First Schedule and Second Schedule as in force immediately before issue of the said notification.

That means, if an item attracts nil rate of duty, it can be made liable to duty to an extent of 50% of its value. For the goods with an existing tariff rate, the rate can be increased to double the rate. E.g. if the existing rate is 10%, it can be increased to 20%.

Conditions

Every notification is to be laid before each House of parliament as soon as may be, if in session and if not, within 7 days of reassembly followed by a resolution seeking parliament's approval within 15 days of such laying.

A notification once issued cannot be substituted by another before the earlier notification receives Parliament approval.

Customs: Central Govt. can exercise similar power under Customs also. Under section 8 of Customs Tariff Act, it can impose or increase export duty. It can also increase import duty under Section 8A. **But under Customs, there is no upper limit prescribed.**

The classification under CETA is based on International Convention of Harmonised System of Nomenclature (HSN) called Harmonised Commodity Description and Coding System. This is an international Nomenclature standard adopted by most of the countries in the world. This was adopted for ensuring uniformity in classification in international trade. The HSN system is scientific and flexible. It helps in reducing classification disputes. Though it was adopted originally for Customs Act, it has been incorporated in excise through Central Excise Tariff Act, 1985 with necessary modifications.

RULES FOR INTERPRETATION (COMMON FOR EXCISE AND CUSTOMS)

There are 6 rules of interpretation (General Interpretation Rules-GIR) which should be applied to determine the classification in cases where it is not possible to classify goods with the help of chapter notes and tariff schedule. If it is still not possible with rules, then apply the principles and guidelines given by the courts.

The rules are given below. These Rules are very important to understand the concept, process and scope of classification of goods.

RULE 1

Rule of Interpretation will come into play only when the classification can not be determined according to the terms of the headings and any relative Section or Chapter Notes. If classification is not possible in accordance with these rules then apply the other rules.

RULE 2(A)

Any reference in a heading to an article shall be taken to include a reference to that article incomplete or unfinished, provided that, as presented; the incomplete or unfinished article has the essential character of the complete or finished article. It shall also be taken to include a reference to that article complete or finished (or failing to be classified as complete or finished by virtue of this Rule), presented unassembled or disassembled.

Classification applicable for completed/ finished/ assembled goods will also be applicable for incomplete or unfinished or unassembled [Semi Knocked down (SKD)/ completely knocked down (CKD)] goods, if such goods have the essential characteristics of finished goods.

However, the incomplete goods must be capable of performing the same functions of completed goods. e.g. Motors vehicle not yet fitted with the wheels or tyres can be classified as motor vehicle.

- (i) In **Shirke construction Equipment P.Ltd.**, bulky crane was cleared in SKD condition in two consignments. Held the assessee cleared the crane in parts and NOT parts of crane. Hence the parts are to be classified as crane.
- (ii) The assessee imported components of colour TV in a series of consignments over a period of 2 years. The Supreme Court held that the parts cannot be classified as colour TV in unassembled form as the components require complicated process to make the colour T.V. These can be classified only as components. **[SONY INDIA, (S.C)]**

RULE 2(B)

Any reference in a heading to a material or substance shall be taken to include a reference to mixtures or combinations of that material or substance with other materials or substances. Any reference to goods of a given material or substance shall be taken to include a reference to goods consisting wholly or partly of such material or substance. The classification of goods consisting of more than one material or substance shall be according to the principles of Rule 3.

Example: Gold with copper will be classified as 'Gold' Plastic bucket with iron handle to be classified as plastic article.

But if such goods consist of more than one material or substance and each substance is equally significant, classification shall be made according to the principle specified in Rule 3.

RULE 3

When by application of Rule 2 (b) or for any other reason, goods are, *prima facie*, classifiable under two or more headings, classification shall be affected as follows:

- (a) The heading which provides the most specific description shall be preferred to headings providing a more general description. However, when two or more headings each refer to part only of the materials or substances contained in mixed or composite goods or to part only of the items in a set put up for retail sale, those headings are to be regarded as equally specific in relation to those goods, even if one of them gives a more complete or precise description of the goods.

Example: VIP bag may be a plastic item. But there is specific tariff heading No (42.02.) for suits cases. Hence, it should be preferred and classified as suit cases.

Similarly, watch straps can be manufactured from metals, plastic, leather etc. All watch straps irrespective of the materials of construction are classifiable under heading No. 91.13. because a specific entry is available for that (*Desai Trading Co. v CCE*)

- (b) Mixtures, composite goods consisting of different materials or made up of different components, and goods put up in sets for retail sale, which cannot be classified by reference to Rule 3 (a), shall be classified as if they consisted of the material or component which gives them their essential character, insofar as this criterion is applicable.

This is applicable where Rule 2 (a) creates conflict and Rule 3 (a) is not possible. If goods consist of different materials and such mixture or combination has no specific heading, it cannot be classified under Rule 3 (a). Classify such goods based on their essential character that is classify such composite product as per the material which gives the product the essential character. Value of the material or component is not relevant for determining essential character. *[Plasturon Processors Ltd.]*

- (c) When goods cannot be classified by reference to Rule 3 (a) or 3 (b), they shall be classified under the heading which occurs last in numerical order among those which equally merit consideration.

If two or more headings appear equally specific, and Sub Rules 3 (a) and (b) cannot be applied, the heading which occurs last in the numerical order is to be taken for classification..

Example: Electrical insulating self adhesive tape can be classified as self adhesive tape under 39.19 and it can also be classified as electrical insulator under 85.46. Then the latter of the two i.e 85.46 will be taken as the classification number. This is popularly called as 'the latter the better' (ie. the last one is the best one)

But under service tax vide Section 65A, the principle of 'the earlier, the better' (ie. the first one is the best one') is applied.

RULE 4

AKIN RULE: If it is not possible to classify by any of the Rules above then classify under the heading appropriate to goods to which they are most akin, i.e. goods be classified under the description where they are closely related to the description in the tariff.

When the classification of comparable goods is applied, care should be taken to see that the goods under comparison must be closely related, i.e. close relation here means functional relation.

RULE 5

In addition to the foregoing provisions, the following Rules shall apply in respect of the goods referred to therein:

- (a) Camera cases, musical instrument cases, gun cases, drawing instrument cases, necklace cases and similar containers, specially shaped or fitted to contain a specific article or set of articles, suitable for long-term use and presented with the articles for which they are intended, shall be classified with such articles when of a kind normally sold therewith. This Rule does not, however, apply to containers which give the whole its essential character.
- (b) Subject to the provisions of Rule 5 (a) above, packing materials and packing containers presented with the goods therein shall be classified with the goods if they are of a kind normally used for packing such goods. However, this provision is not binding when such packing materials or packing containers are clearly suitable for repetitive use.

RULE 6

For legal purposes, the classification of goods in the subheadings of a heading shall be determined according to the terms of those subheadings and any related Subheading Notes and, *mutatis mutandis*, to the above Rules, on the understanding that only subheadings at the same level are comparable. For the purpose of this Rule the relative Section and Chapter Notes also apply, unless the context otherwise requires.

TIPS FOR CLASSIFICATION

1. *Classification not possible as per tariff schedule - use chapter notes/ section notes.*
2. *Not possible with chapter notes/ section notes - apply General Interpretation Rules.*
3. *If not possible even with Rules for interpretation - follow guidelines given by courts.*

TRADE PARLANCE TEST

The first and foremost principle to be applied is trade parlance test/ popular test. When the classification is not possible even as per rules, guidelines provided by the courts must be referred. The courts have

consistently held from time to time that trade parlance test must be preferred to technical or dictionary meanings of the words.

When trade parlance test fails other options including BIS (Bureau of Indian Standards) classification may be tried. However trade parlance test cannot be applied where classification is possible under the rules for interpretation.

Timing of classification: Procedures start with classification as the goods manufactured or imported must be classified for registration/clearance. Liveability of goods is determined on the basis of classification applicable at the time of manufacture. However, dutiability of goods is decided as per the rate of duty on the date of such removal.

Change of Classification No: When there is a change in classification No. after manufacture but before removal of goods, the latest Classification No prevailing at the time of removal is to be applied. Even those goods attracting Nil rates at the time of manufacture may become dutiable at the time of removal due to the subsequent change in classification.

CASE LAWS UNDER CLASSIFICATION

1. *Commissioner of Central Excise, Bhopal v. Minwool Rock Fibres Ltd. 2012 (278) E.L.T. 581 (SC)*

Facts: Minwool Rock Fibres Ltd. started manufacturing rockwool and slagwool using more than 25% of blast furnace slag by weight in 1993. They classified them under Central Excise Tariff heading 6803.00 (i.e. Slagwool, Rockwool and similar mineral wools) and had been filing classification declarations mentioning this fact. Such declarations so filed prior to 1997-98 were accepted by the Department. However, another specific sub-heading 6807.10 of the Central Excise Tariff was introduced vide Budget 1997 for '*Goods having more than 25% by weight blast furnace slag*'. Accordingly, they claimed that the goods manufactured by them, namely, slagwool and rockwool should henceforth be classified under Chapter sub-heading 6807.10 of the Tariff.

Issue: The assessee's contention was that the appropriate classification for their product was under Chapter sub-heading 6807.10 of the Act while the Department contended that the appropriate classification was under Chapter sub-heading 6803.00 of the Act.

This was the subject matter of the appeal before the Supreme Court.

Decision: Tariff heading specifying goods according to its composition should be preferred over the specific heading. Sub-heading 6807.10 is specific to the goods in which more than 25% by weight, red mud, press mud or blast furnace slag is used as it is based entirely on material used or composition of goods.

Therefore, the Court opined that the goods in issue were appropriately classifiable under Sub-heading 6807.10 of the Tariff.

2. JOCIL LTD. (S.C), 2011

Non edible industrial grade crude palm stearin was imported and the assessee classified it under heading 1511 as '*other palm oil, whether or not refined*'.

The department objected to it and classified it under heading No.38 23 as '**RBD PALM STEARIN**'.

The tribunal by applying the principle of essential character as per Rule 3(b), held that it is classifiable as other palm oil since major content in the product is palm oil.

The Supreme Court reversed the order of the tribunal and applied the principle of specific description under Rule 3(a).

Reasons: 1. Chapter 15 deals with edible oils. This product is non edible. 2. This product has a specific heading under chapter 38. Where specific heading is available, principle of essential character under Rule 3 (b) should not be considered. Hence, the classification made by department under Tariff No.38231112 is correct.

3. CHAMPDANY INDUSTRIES LTD. 2009 (S.C.) : Carpets are being manufactured **predominantly** by jute with the surface of polypropylene. As per section note to the chapters, it was held that the carpet should be classified as jute carpet.

4. LAL DANTMANJAN manufactured by BAIDYANATH AYURVED BHAWAN Ltd. is cosmetics and not a medicine. Hence exemption granted to ayurvedic medicaments is NOT available to Lal Dantmanjan. (CASE: BAIDYANATH AYURVED BHAWAN Ltd ; 2009 (S.C.)

5. VODAFONE ESSAR SOUTH LTD. 2009 (H.C): Assessment was made and duty was paid on imported optic fibre cables (OFC) on the basis of classification No. 85.44...The commissioner (Appeals) decided that OFC is classifiable under heading 85.44. Department filed an appeal before CESTAT claiming that the OFC shall be classified under heading 90.01

DRI [Directorate of Revenue Intelligence] officers of customs also seized the goods and demanded differential amount of duty.

The Bombay High Court held that the action of the Dept. was unwarranted as the goods were properly assessed as per the order of the commissioner (Appeals) and the CESTAT had not set aside the order. Further held that recovery of differential duty is not in accordance with law.

6. Rules for interpretation given under Tariff Act cannot be applied to interpretation of exemption notifications. Exemption notifications shall be interpreted strictly in terms of their language. **[CASE : MEWAR BARTAN NIRMAN UDYOG , 2008 .S.C.]**

7. XEROX (I) LTD. S.C. (2010): Classification of Multifunctional Machine

Issue: whether the multifunctional machine performing the functions of a printer, fax machine, copier/scanner to be classified under tariff No. 8471.60 or 8479.89

Held: 85% of the total parts & components is allocated to printing and printing gives the machine the essential character. Hence classifiable under the heading 84.71.60. Contention of the importer was accepted.

Note: Tariff No. 8471.60 deals with automatic data processing machines and 8479.89 for machines & appliances having individual functions not specified in this chapter.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not be submitted for evaluation).

1. What is classification? Why classification is necessary?
2. Briefly describe the powers of Central Government as listed under Section 3(1) of the Central Excise Tariff Act, 1985.
3. What are the rules for interpretation? Give a brief note.
4. Enumerate the main features of Central Excise Tariff Act, 1985.

SUGGESTED READINGS

- (1) Indirect Taxes—Law & Practice – *V.S Datey, Taxmann*
 - (2) Central Excise Law Manual – *R.K. Jain, Centax Publications, New Delhi*
 - (3) Excise Law Times – *Centax Publication, New Delhi*

CENTRAL EXCISE LAW

PART III: VALUATION OF EXCISABLE GOODS

After completion of this part, students will be well-acquaint with;

- Valuation methodology for the chargeability of excise duty
- Central Excise Valuation Rules, 2000
- How duty is determined
- Related case laws

INTRODUCTION

Goods are required to be assessed at the time of removal after levy of duty at the time of Manufacture. The assessment is made as per the rates specified in Central Excise Tariff Act, 1985. As we are aware, there are two Schedules under Central Excise Tariff Act. The duty levied under the First Schedule is called Basic Excise Duty (BED)/CENVAT and the duty under Second Schedule is SED (Special Excise Duty). If a manufactured item figures in only First Schedule, only CENVAT is levied.

W.e.f 01-03-2006 vide Notification No.9/2006, all the goods falling under Second Schedule to Central Excise Tariff Act, 1985 are exempt from whole of excise leviable thereon.

RATES OF DUTY

Basically, there are two rates of duty levied under Central Excise Act, 1944; specific rates and ad valorem rates. Specific rates are unit rates based on quantity. The base unit may be a kilogram, a centimeter, a quintal, a tonne and so on. Some of the goods and their respective rates are given below:

<i>Excisable Item</i>	Base Unit
Cigarettes	millimetre (Length)/ Number
Cement	Tonne (Weight)
Molasses	Tonne (Weight)
Marble Slab	Square Metre (Area)
Sugar	Quintal (Weight)
Tea	Kilo (Weight)

A very few items attract specific rates under excise law. The specific rates are easy and simple to understand and apply but, there are practical difficulties attached to them. It is not possible to fix rates for all the varieties of goods. They require frequent revision due to price fluctuations. That is the reason why ad valorem rates (i.e. percentage rates based on value of manufactured goods) are in vogue all over the world.

The ad valorem rates have the following advantages:

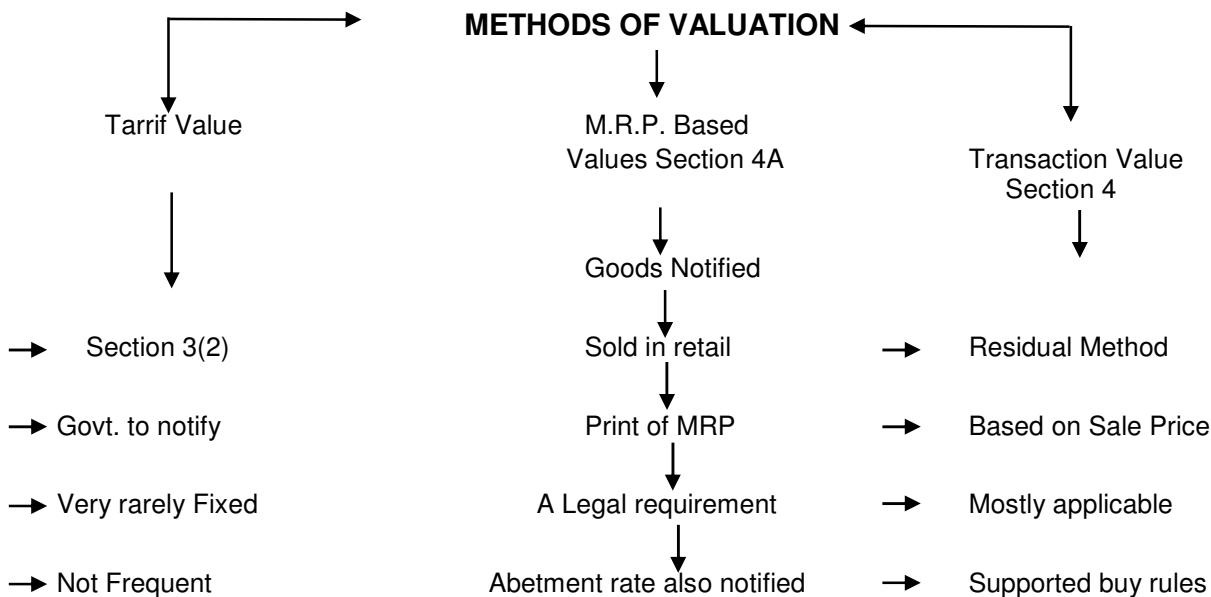
1. They are flexible and elastic
2. They are scientific
3. They are convenient
4. They have in-built adjustability to price and quality variations.

A very few items are valued on specific-cum-advalorem rates e.g. Cigarettes are first assessed at specific rates under Central Excise Tariff Act, again they are valued on ad valorem rates as applied under Additional Duties of Excise (Goods of Special Importance) Act.

METHODS OF VALUATION

Excise Duty is either specific duty or ad valorem duty. The type of duty and the rate of duty applicable is mentioned in the Schedules to Central Excise Tariff Act, 1985. From the above discussion, it is clear that most of the excisable goods are assessed on ad valorem basis. That means goods require valuation and on that value (Known as assessable value), duty amount is calculated at specified percentage rates. There are three methods of valuation under Central Excise Act, 1944:

1. Tariff values under Section 3(2) notified by Govt.
2. MRP based values computed for the goods notified by the govt. under Section 4A.
3. Transaction value under Section 4 where the assessable value under the above two methods is not applicable.



(1) TARIFF VALUES

The Central Government is authorised to notify tariff values of any articles enumerated, either specifically or under general headings, in the First and Second Schedule to the Central Excise Tariff Act, 1985. The tariff value is the notional value. Where the tariff values are fixed under Section 3(2), neither transaction value nor MRP based value can be used for such goods. The following points are relevant for the tariff values:-

- The tariff values are fixed by Central Govt. by notification.
- A few goods are covered under this scheme.
- Different tariff values may be fixed
 - for different classes or description of the same excisable goods or
 - for excisable goods of the same class or description:
 - produced or manufactured by different classes of producers or manufacturers or
 - sold to different classes of buyers.

The main purposes for which the tariff values are fixed are to prevent undervaluation of certain goods and to mitigate litigation.

Basis of Fixation: The values may be fixed by the Government on the basis of (i) whole sale prices or (ii) average of such whole sale prices.

Tariff values have been fixed for the following products:

- For readymade garments under chapters, 61, 62 and 63 where MRP is printed, tariff value shall be taken as 30% of MRP. Transaction value will be taken as tariff value for those having no MRP.
- Tariff values have been fixed for articles of jewellery under heading 7113 other than
 - silver jewellery
 - jewellery manufactured from precious metal/ old jewellery provided by retail customer.

(2) VALUATION BASED ON MRP [RETAIL SALE PRICE] (SECTION 4A)

On 4th November, 1987, the Collector's (Excise) Conference was held. It was suggested in the conference that retail price instead of wholesale price should form the basis of valuation for assessment of excise duty for such commodities which show a difference of more than 100% between the retail price and the wholesale price. The Board consequently, called for details of such commodities. It took nearly a decade to translate the proposal into a reality. The budget 1997 finally introduced the system. Section 4A was inserted in the Central Excise Act and the valuation based on retail price came into effect on 14th May, 1997. This novel concept of assessment of duty on consumer goods met with a thumping success.

Under this scheme, Central Government is authorised to notify certain goods sold in a packaged form having MRP printed on them. The Legal Metrology Act, 2009 and Legal Metrology (Packaged Commodities) Rules, 2011 made there under, require the packaged commodities to bear the maximum retail price (MRP). Out of such packaged commodities, some of them have been notified by the govt. from time to time and such commodities notified by the govt. are valued under Section 4A of the Central Excise Act, 1944.

SCHEME OF VALUATION

The notified goods should necessarily bear the MRP. The MRP declarations are statutorily required where the printing of MRP is statutory and not compulsory, or where the assessee prints the MRP voluntarily, such goods need not be valued under Section 4A even though the goods are notified by the Government for this purpose. The MRP is the basis for arriving at assessable value. Rates of abatement are notified by the Government. Rates of abatement may be different for different commodities.

The assessable value = MRP – Abatement value.

The amount of duty is percentage of duty mentioned in the Schedules to Central Excise Tariff Act.

Example

Mineral water under classification No. 2201 carry 45% abatement and the First Schedule to the Central Excise Tariff Act specifies 12% and 3% basic duty and education cess respectively on mineral water. Find out the amount of duty if the MRP of a bottle is ₹15

Solution: The amount of duty payable on a bottle with MRP of ₹15 is calculated as follows:

The assessable value is ₹ 8.25 (15- 6.75). The duty amount on ₹ 8.25 is ₹1.02 i.e., 12.36% of ₹8.25

Example

Refrigerators under classification No.8418.21 carry abatement rate of 38% and they are specified only in Schedule I. Find out the amount of duty if the MRP of a refrigerator is ₹20,000.

Solution: Assessable value is 62% of ₹20,000 i.e. ₹12,400. The amount of duty is ₹1533 (assuming 12.36% duty on ₹12,400).

SCOPE AND OBJECTS

Section 3(2) overrides Section 4. Section 3(2) and Section 4A are mutually exclusive. Same goods are not subjected to tariff values as well as valuation under Section 4A. The main objectives of valuation are:

- To discourage the practice of manufacturers offering high margins to the retailers by printing higher MRPs.
- To augment revenue collections by levying duty on post removal expenditure like, advertisements, transportation, middle men's profits etc.
- To simplify the process of valuation finally to reduce litigation.

Section 4A overrides Section 4. It means transaction value cannot be adopted for the valuation of goods notified under Section 4A [Section 4A(2)].

Even if the goods are manufactured by a job worker, the valuation of goods must be done under Section 4A only when the goods are notified under this section.

Section 4A(4) specifies that where goods under this section are removed without declaring MRP or MRP declared is not as per law or Obliteration, tampering or alteration of price after removal the goods are liable to be confiscated and retail price in such cases will be ascertained in the prescribed manner.

DETERMINATION OF RETAIL SALE PRICE

The application of MRP based valuation is subject to the Central Excise (Determination of Retail Sale Price of Excisable Goods) Rules, 2008 notified vide Notification No.13/2008, dated 01-03-2008. For the purpose of Rule 4A(4), the retail sale price shall be determined as follows:

(A) Price not declared or declared but not as per law or obliterates after removal (Rule 4):

- (a) Where a manufacturer removes the goods under Section 4A(1) without declaring the retail price; or
- (b) Declared price is not as per law; or
- (c) Obliterates the price after removal from place of manufacture.

Then the price is ascertained in the following manner:

- (i) take market price of identical goods removed by the manufacturer within a period of one month before or after removal of such goods.
- (ii) if the retail price can not be ascertained as above, it shall be ascertained by conducting market enquiries in the retail market.

If more than one retail price is ascertained in the above cases, the highest of them shall be taken for assessment.

(B) Price altered or tampered:

If the manufacturer alters or tampers the price after removal and it results in increase of retail price, then

- such increased price shall be taken as price for all goods removed one month before and after the removal of such offended goods.

If the alteration or tampering results in increase of more than one price, the highest of them shall be taken.

(C) Price cannot be ascertained:

If the price cannot be ascertained under the above rules [Rules 4 & 5], it shall be ascertained as per the provisions under Section 4A as follows:

- If a package contains different MRPs printed on it, highest of them must be taken for the purpose of valuation.
- If declared retail sale price altered at the time of the clearance from the place of manufacture, to increase the retail sale price then such altered retail sale price shall be deemed to be the retail sale price.
- If separate MRPs are printed on packages meant for sale in different places, each of such MRP is taken for the purpose of valuation and each such consignment is valued separately.

Meaning of Retail Sale Price [Explanation 1 to section 4A(4)]:

"Retail Sale Price" means the maximum price at which the excisable goods in packaged form may be sold to the ultimate consumer and includes all taxes local or otherwise, freight, transport charges, commission payable to dealers, and all charges towards advertisement, delivery, packing, forwarding and the like, as the case may be, and the price is the sole consideration for such sale.

Explanation 2 to section 4A (4)

- (a) Where more than one MRP is printed on a package, highest of such MRPs shall be taken for valuation.
- (b) Where MRP is altered to increase the price at the time of removal, the increased price shall be taken as the retail sale price.(MRP)
- (c) Where different MRPs are declared on different packages meant for sale at different places then each of such retail price shall be taken for valuation.

Example: Clean Tooth Ltd. Manufactures tooth pastes at its factory in Nagpur. The following maximum retail prices (MRP) are printed on the packet

MRP in Punjab	:	₹35
MRP in Assam	:	₹37
MRP in other places	:	₹33

Abatement rate is 30%. Total number of units removed from factory is 100,000.

Excise duty as per Tariff Act is 12% education cess is payable. Find out excise duty payable on the entire quantity removed.

Solution: As per explanation 2(a) of Section 4A(4) ₹ 37 shall be taken as MRP.

Hence assessable value (70% of MRP) = ₹25.9

Total value = ₹ 25,90,000

Excise duty = $\frac{25,90,000 \times 12.36}{100}$
 = ₹ 3,20,124

Important Notes:

(1) *Free samples or physician samples for goods notified under Section 4A shall be valued based on the MRP declared on such goods*

CBEC issued a circular in Feb, 2010 (No. 915/05/2010) declared that value of physician samples would be the value determined under Section 4A for the identical goods. (subject to adjustments for size and pack)

Larger bench of tribunal in CADILLA LABORATORIES, 2008 held that physician samples shall be valued at MRP less abatement of such goods.

Further, the circular states that the decision of the tribunal would be more or less applicable in respect of free samples of other products under MRP assessment.

(2) MRP based valuation scheme is not applicable to the following:

- Exports
- Bulk sale/sale in wholesale pack.
- Package of less than 10 gram/ 10 ml.
- Sale to industrial / institutional consumers.
- Hence, transaction value method under Section 4 is applicable for above.

Circular Information:

1. Quantity discount, bonuses etc. are applicable for the valuation of goods under section 4 of the Central Excise Act, 1944 and not in case of goods valued under Section 4A. (Circular No. 938/28/2010 CX dt. 29-11- 2010)
2. In case MRP is scored out and new MRP is printed with reduced price, the reduced price is accepted for valuation. (Circular No.673/ 64/2002 CX dt. 28-10- 2002)

CASE STUDIES

(1) KRAFTEC PRODUCTS INC. 2008 (S.C.): Multi piece packets whose total weight is less than 10 grams are liable to be valued under Section 4 and not under Section 4A. Even though they have been notified by the govt. under Section 4A.

KRAFTEC manufactures hair dye. It is packed in 3 pouches of 3 gms and sold in one packet. The net weight of each pouch, as also the net weight of the commodity in 3 pouches and the maximum rate is printed on the pouches.

Note: As per Packaged Commodity Rules, the retail packs below ten grams/10 ml. are exempt from printing MRP on them. Where MRP is not a statutory requirement, Section 4A can not be applied.

(2) JAYANTI FOOD PROCESSING (P) LTD. 2007 10 STT 375 S.C. HELD that ice cream supplied in the

four litre pack to hotels is a wholesale pack and not retail pack. As such, the goods have to be assessed under Section 4 and NOT Section 4A.

Vide department circular No.873/11/2008, dt. June 24, 2008, the department accepted the above decision.

(3) Whirlpool of India Ltd. v. Union of India - 2007 (218) E.L.T. 167 (S.C.): Even if the package of refrigerator is required to be opened for testing, it would be pre-packed commodity subject to MRP based valuation.

TARIFF VALUE v. MRP BASED VALUE

Notification	: Values are notified	Goods are notified
Computation	: Values are readily available	Values are found out by deducting the abatement rates from the MRP
Values	: Tariff value is a notional value	This is a computed value only abatement rates are notional
Item	: Any item can be picked up for Declaration of Tariff Value	Only those items requiring MRP declaration under any law in force
Base	: Wholesale/market/average price	MRP is the base
Purpose	: To defeat undervaluation to mitigate litigation	To discourage over statement of MRP to augment revenue collections

(3) VALUATION BASED ON TRANSACTION VALUE (SECTION 4)

If a product is not notified under section 4A and there is no tariff value fixed for it under section 3(2), it has to be assessed according to its transaction value determined under section 4 as substituted with effect from 1-7-2000.

The law pertaining to determination of assessable value for excisable goods is contained in Section 4 of the Central Excise Act, 1944, supplemented by the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000. Section 4, as it exists now, has been introduced into the statute by an amendment made by the Finance Act, 2000, and brought into force w.e.f. July 1, 2000 on which date the Valuation Rules were also simultaneously brought into force.

HISTORY AND BACKGROUND

Transaction Value is a new entrant into the portals of Excise. It was introduced in the year 2000 with effect from 1st July 2000. It is a simple and well nurtured concept.

Transaction Value's birth was as a result of years of rich experience with valuation methods till 1-7-2000. Earlier, the assessable value was based on wholesale price. It was drafted on the lines of Section 30 of the Sea Customs Act, 1878. Section 4 was restructured and the concept of normal price was introduced with effect from 1.10.1975. After undergoing the orders of judicial review for 25 years, and when almost every issue of contention was settled, it was finally decided to bid farewell to the Normal price and Transaction Value was called upon to replace it. The new entrant has two distinct features: First, the assessable value under the earlier schemes was based on notional values. Now, it is under actual transaction value. Second, single uniform price was made applicable to each class of buyers in wholesale trade. Under the new

method, each removal is considered a separate transaction and its transaction value is taken as assessable value. In brief, Transaction Value is based on actual invoice price, not on notional price.

The concept of transaction value had its roots as early as in 1975. This was sparsely applied to goods falling under residual tariff item No.68 existing prior to the enactment of Central Excise Tariff Act, 1985. Exemption Notification No.120/75-CE dt. 30-6-1975 allowed the application of transaction value as given below:

“..... The Central Govt. hereby exempts goods falling under item No.68 of the First Schedule to the Central Excise Act, 1944, cleared from the factory of manufacture, on sale, from so much of the duty of excise leviable thereon as is in excess of the duty calculated on the basis of the invoice (excluding duty and local taxes, if any, included in such price) charged by the manufacturer for the sale of such goods”.

What was allowed earlier under exemption as a special case is being applied now as a universal application. But the Revenue has taken a quarter century to come to the finality. The honourable Finance Minister on the budget day in the year 2000 declared:

‘I want to make the valuation mechanism simpler, user-friendly and also commercially acceptable. From 1st July, 2000, I propose to replace the existing Section 4 of Central Excise Act, which is based on concept of normal price by a new section based on transaction value for assessment. This is a path breaking departure from the traditional approach.

Indeed, the introduction of Transaction Value is a path breaking venture. It is also claimed by the Revenue that the main purposes of the replacement are to simplify the process of valuation; to honour and incorporate the relevant rulings of courts. But there is perhaps yet another predominant purpose – i.e. to augment revenues.

Note:

The substitution of the concept of assessable value from “Normal Wholesale Price” to “Transaction Value” has been made to make the valuation mechanism simple, user friendly and on commercially accepted lines. Besides, it has been termed as a move to facilitate the introduction of full-fledged VAT in place of CENVAT as introduced in Central Excise Law through Union Budget, 2000.

The current Section 4 closely follows the prescription regarding assessable value to be based on ‘Transaction Value’ in the first instance as in Section 14 of the Customs Act, 1962. The Customs concept, in turn, is inspired by the Brussels Concept of Value i.e. the concept of assessable value in commodity taxation, conceived and devised by the Customs Co-operation Council (CCC) (now renamed as World Customs Organisation) Headquartered in Brussels, Belgium. It is noteworthy that it is the WCO which is the author of the Harmonised System of Nomenclature which forms the basis of the Excise and Customs Tariffs in India.

PROCEDURE FOR DETERMINATION OF TRANSACTION VALUE UNDER SECTION 4

Section 4 of the Central Excise Act, 1944 advocates valuation of goods on the basis of Transaction Value. Section 4(1) provides that where the duty of excise is chargeable on any excisable goods with reference to their value, then, on each removal of the goods, such value shall—

- (a) In a case where the goods are sold by the assessee, for delivery at the time and place of the removal, the assessee and the buyer of the goods are not related and the price is the sole consideration for the sale, be the transaction value.
- (b) In any other case, including the case where the goods are not sold, be the value determined in such manner as may be prescribed.

In other words, when duty is charged on value of goods sold, its Transaction Value (adjusted sales value) is the assessable value of such sale. Each removal of goods is distinct and has a Transaction Value of its own i.e. different removals may have different Transaction Value. For Transaction Value to be accepted as the assessable value following three conditions must be satisfied:

1. The goods are sold by the assessee for delivery at the time and place of removal;
2. The assessee and the buyer are not related; and
3. The price is the sole consideration for the sale.

If any of these three conditions is not fulfilled, Transaction Value is not accepted and valuation rules apply in such cases.

Hence, the transaction value cannot be applied in the following cases:

- *When there is no sale;*
- *There is sale, but it is made to a related person or sale and delivery are not from the place of removal.*
- *Consideration in such sale is not the sole consideration.*

Scheme of valuation under section 4 in a nutshell: - This is a residual method. It is applied when excisable goods cannot be assessed under all other methods.- This method is based on actual sale price.

ANALYSIS OF SECTION 4(1)(A)

This section lays down the conditions necessary to be fulfilled to apply transaction value directly without the use of Rules.

1. Goods must be sold for delivery at the time and place of removal:

It means:

- (i) there is sale at the time of removal; and
- (ii) such sale is for delivery at the place of removal i.e. place of removal and place of delivery are same. Obviously, the price is ex-factory price and ownership is changing hands at the place of removal itself.

The place of removal has been defined under Section 4(3)(c) as,

- *a factory or any other place or premises of production or manufacture of the excisable goods;*
- *a warehouse or any other place or premises wherein the excisable goods have been permitted to be deposited without payment of duty;*
- *a depot, premises of a consignment agent or any other place or premises from where the excisable goods are to be sold after their clearance from the factory from where such goods are removed.*

Sales depot, place of consignment agent, branch office etc. are brought within the purview of the place of removal under the new definition but the sale from them is governed by Rule 7 of Valuation Rules.

Assessee has been defined as a person who is liable to pay duty under this Act and includes his agent. [Section 4(3)(a)].

In conclusion, the first condition is satisfied when :

- there is sale at the time of removal;
- the delivery is from factory / warehouse;
- such delivery is for the purpose of sale from the factory or warehouse.

2. Assessee and Buyer are not related:

Even if there is sale, the transaction value on such sale is not acceptable if the assessee (manufacturer) and the buyer are related. Section 4(3)(b) clarifies that persons shall be deemed to be related if-

- they are inter-connected undertakings (definition is given at annexure at the end of this part);
- they are relatives;
- amongst them the buyer is a relative and distributor of the assessee, or a sub-distributor of such distributor; or
- they are so associated that they have interest, directly or indirectly in the business of each other.

3. Price is the sole consideration

The price paid by the buyer may not be the sole consideration. There may be some other considerations in addition to the price. If there is any other consideration that could possibly influence price, the assessable value has to be determined under Rule 6.

When there is a sale from the factory/ warehouse at the time of removal of goods and such sale is made for full commercial consideration to an unrelated person, such sales value is accepted as transaction value. Otherwise, valuation is made according to Valuation Rules, 2000.

4. Transaction Value defined under section 4(3)(d)

‘Transaction value’ means the price actually paid or payable for the goods, when sold, and includes in addition to the amount charged as price, any amount that the buyer is liable to pay to, or on behalf of, the assessee, by reason of, or in connection with the sale, whether payable at the time of the sale or at any other time, including, but not limited to, any amount charged for, or to make provision for, advertising or publicity, marketing and selling organisation expenses, storage, outward handling, servicing, warranty, commission or any other matter but doesn’t include the amount of duty of excise, sales tax and other taxes, if any, actually paid or actually payable on such goods”.

Ingredients of transaction value are:

- *It is the price actually paid or payable for the sale of goods.*
- *It is the price realized on sale.*
- *It includes any amount the buyer is liable to pay.*
- *It includes any amount liable to be paid on behalf of the assessee.*
- *The amount should be by reason of or in connection with the sale.*
- *It may be payable at the time of sale or any other time.*
- *It includes but is not limited to any amount charged for advertising, marketing, publicity, storage etc.*
- *It doesn’t include the duty of excise, sales tax and other taxes.*

- *The transaction value is of wider import. It includes many things which were agitated earlier before the courts under the old provisions of valuation.*
- *The transaction value doesn't even have the mention of certain terms like packing expenses, discounts and so on. Yet, it can be interpreted that the transaction value is the net realizable sale price, after deducting all the discounts under normal trade practice.*
- *The packing expenses if any, are automatically included in the transaction value. Only the durable, returnable packing expenses charged from the buyer may be eligible for deduction.*
- *The concepts, such as post manufacturing expenses, post removal expenses propounded in Bombay Tyres International and MRF Ltd. cases respectively, have no direct bearing on the definition of transaction value. This definition is wide enough to include even post-removal expenses. E.g. after sales service charges collected from the buyer.*

Deductions: Only excise duty and sales tax have direct mention as deductions, though of course, interest on delayed payments is not part of the transaction value. Discounts allowed in the normal trade needs no special mention as the concept of Transaction Value is the net amount that is payable by the buyer after all such deductions.

- The terms such as liable to pay 'by reason of, or in connection with sale' are not defined. They may necessitate judicial interpretation. The definition has given ample scope to the department to claim variety of items to be included in the transaction value which the assessees may find difficult to cope with.
- The definition lays emphasis on what is payable by the buyer for the purchase of goods. The nature of such payments, whether it relates to manufacturing, selling, post manufacturing, post selling etc. is irrelevant now. The amount is includable if it is by reason of or in connection with sale.
- It may be noted that any amount spent by the buyer on his own account (eg. Advt.) and not payable to the seller because of sale, is not includable in the assessable value. In LML Ltd. v. CCE, 2001 (129) ELT, the Tribunal held that in case of common share of advertisement expenses, only seller's share of advertisements is includable in assessable value.
- Regarding the notional interest on advances paid by the buyer, the Supreme Court held in Metal Box case that notional interest is to be added to the price when there is nexus between sale and such advance i.e. when the advance influences the price.
- Conversely, in VST Industries v. CCE, 1998, the Supreme Court held that if the price charged from all the customers is same though some customers have advance deposits with the company, the notional interest need not be loaded into the price as the advances have no influence on price.

INCLUSIONS & EXCLUSIONS FOR DETERMINING TRANSACTION VALUE

CBEC Circular No 354/81/2000: This is a master circular released with the introduction of Valuation Rules, 2000.

As per the circulars and case law the following points are relevant: -

1. Sale price, obviously is after deducting all the discounts.
2. The packing expenses if any are automatically included in the transaction value. Only the durable and returnable packing expenses charged from the buyer are eligible for deduction.
3. Pre-delivery inspection charges, dharmada charges, royalty charges are also includable in value .
4. Erection /installation bringing about immovable property are not included in value. Octroi and other taxes are not to be included as they are in the nature of taxes.

5. Interest on delayed payments is not includable.
6. Duties and taxes actually paid or payable are to be excluded.
7. Bought out accessories cost is not includable if they are not essential part of the main product.
8. Advertisement charges borne by the buyer are not deductible from value as they are part of purchase price.
9. subsidies given by Govt. to the manufacturer need not be included in transaction value

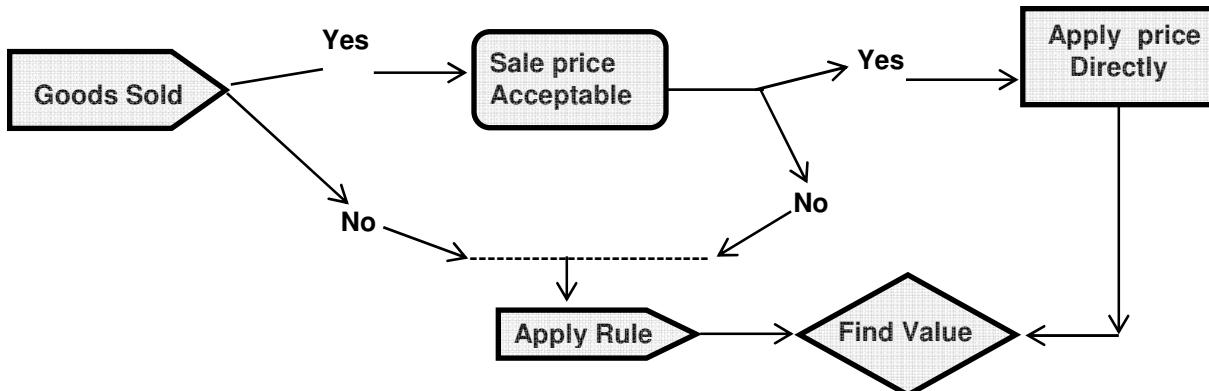
Circular No. 936/26/2010 CX Dt. 27th October.

The larger bench of CESTAT vide its order dated 13.8.2010 in appeal No. 1958 of 2008 in the MARUTI UDYOG LTD case, has held that Pre-delivery Inspection charges and After-sale Service charges collected by the dealers are to be included in the assessable value under Section 4 of the Central Excise Act, 1944.

CENTRAL EXCISE VALUATION [Determination of Price of Excisable Goods] Rules, 2000

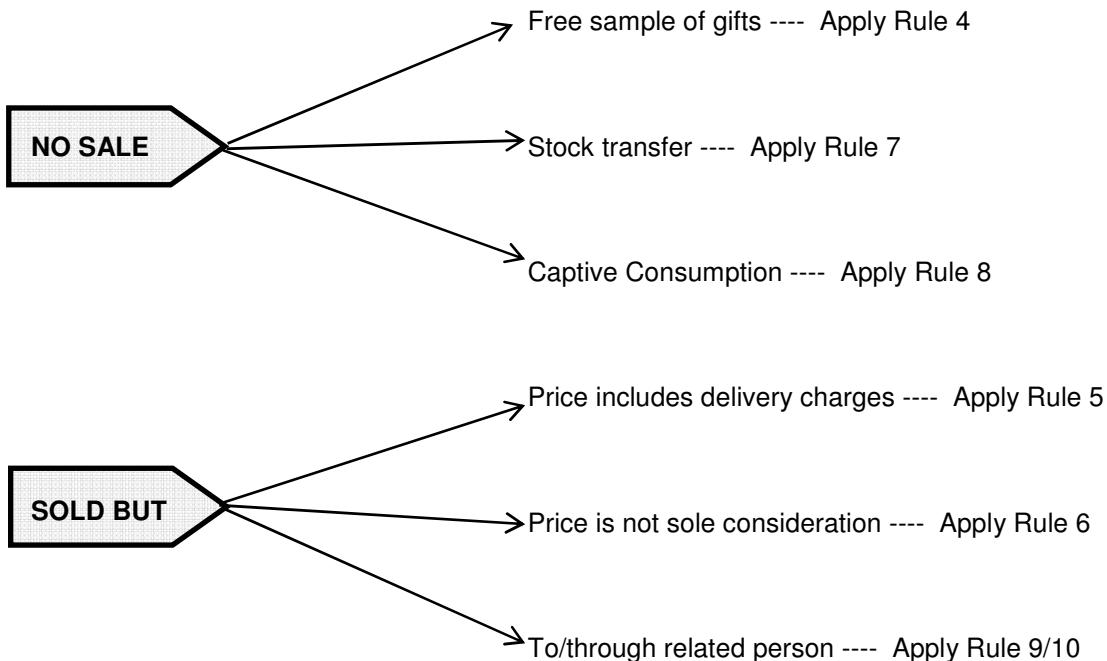
RULE 1	Applicability
RULE 2	Definitions
RULE 3	Apply rules where transaction value cannot be applied
RULE 4	No sale at the time of removal
RULE 5	Place of delivery is other than the place of removal and the price includes transport charges from factory
RULE 6	Price is not sole consideration
RULE 7	Stock transfer
RULE 8	Captive consumption
RULE 9	Related person transactions
RULE 10	Relaxation in related person transactions
RULE 10 A	Goods manufactured by a job worker
RULE 11	Residual method/ best judgment method.

APPLICABILITY OF TRANSACTION VALUE



1. Where there is sale and the price is acceptable under Section 4(1)(a), apply the price directly.
2. Where there is no sale/there is sale but price not acceptable, apply Rules [Section 4(1)(b)]

VALUATION RULES, 2000



This rule is not applied in case of stock consumption and captive transfer, even though, there is no sale in those two situations. For them there are separate rules i.e. Rules 7 and 8 respectively.

It may be noted that in a circular issued by the Board, it was specified that for gifts and free samples, Rule 4 is applicable.

But if the goods are those notified under Section 4A, value shall be based on the MRP.

RULE 4 - WHEN THERE IS NO SALE AT THE TIME OF REMOVAL:

When there is no sale at the time of removal, sale price is not available. Naturally, transaction value is not available. Then, the following methodology is prescribed under Rule 4.

- Take the price of such goods sold at the time nearest to the time of removal.
- Make reasonable adjustments. These adjustments may be with reference to any price fluctuations during the time lag between these two removals, difference in the quality, and packing material used and so on.

RULE 5 - DELIVERY FOR SALE NOT AT THE PLACE OF REMOVAL:

Rule 5 is applicable when there is a sale at the time of removal, but delivery is not at factory, but at some other place, say, and the place of buyers. This is a situation where price is quoted in the invoice includes freight and insurance charges. Since, the price is not ex-factory price, transaction value cannot be applied. Hence, valuation is done under Rule 5.

Conditions necessary for the application of Rule 5:

- Place of removal and place of delivery are not same.
- Price quoted is, inclusive of the cost of transportation and insurance from the factory to the place of buyer.
- The price for the purpose of valuation will be the price charged from the buyer
- If the manufacturer uses his own vehicles freight charges as certified by a C.A./ CWA are allowed to be deducted from the price.

In Circular No. 923/13/2010 – CX , 19th May, 2010. CBEC gave a clarification:

The decision given by CESTAT in Gujarat fluorochemicals Ltd. [2009 (248) E.L.T. 885 has been accepted by the BOARD. Accordingly the clarification issued by the Board vide circular No 634/34/2002-CX dated 1st July 2002 as amended is withdrawn and it is clarified that cost of return fare of vehicles is not required to be added for determining value. (Vide Rule 5 of Valuation Rules, 2000).

Equalised freight (CAS 5): This is an average of the freight charges allowed to be deducted uniformly for all sales to different destinations. This is possible only when the sale is from factory.

Illustration for calculation of equalized freight

A manufacturer has factory at Hyderabad. He has uniform price of ₹ 1,000 (excluding taxes) per unit for sale all over India.

During 2013-2014 he made the following sales:

<i>Place of delivery</i>	<i>No. of units</i>	<i>Transportation Charges</i>
<i>Chennai</i>	<i>500</i>	<i>15,000</i>
<i>Delhi</i>	<i>700</i>	<i>50,000</i>
<i>Ahmedabad</i>	<u><i>800</i></u>	<u><i>25,000</i></u>
<i>Total</i>	<u><i>3,000</i></u>	<u><i>90,000</i></u>

What is the assessable value?

Solution:

$$\text{Average charges per unit} = \frac{90,000}{3,000} = ₹ 30/-$$

$$\therefore \text{Assessable value per unit} = (1,000 - 30) = ₹ 970/-$$

Important note:

Rule 5 is applicable to cases where sale concluded at factory or warehouse and the price included the freight and insurance charges upto the place of customer. In such a case only actual freight charges incurred have to be deducted from the price charged. Any profit made on transportation becomes taxable.

Illustration: There is an agreement for sale of machinery manufactured by X Ltd. at Delhi for a price of ₹70,00,000 which includes transport charges upto the place of customer located in Kanpur.

X Ltd. paid ₹60,000 to the transporter towards transportation charges upto Kanpur.

X Ltd. Charges ₹69,00,000 for sale and delivery of such machinery at Delhi.

Rate of duty is 12% and education cess as applicable.

Find out the assessable value and duty payable.

Solution: Rule 5 is applicable in this case as the price is inclusive of transportation charges. As per Rule 5, only actual transport charges incurred are allowed as deduction. Hence, price for the purpose of valuation shall be ₹69,40,000 (70,00,000 — 60,000)

$$\text{Assessable value} = \frac{69,40,000 \times 100}{112.36} = ₹61,76,575$$

$$\text{Duty Payable} = \frac{69,40,000 \times 12.36}{112.36} = ₹7,63,425$$

The table given below gives an idea on Treatment of profit on transportation charges:

(1) Sale at the place of removal but the price is cum-duty price and it includes transport charges upto the place of customer	Deduct only actual transport charges. Any transport charges collected by adding profit, such profit element should be added back to transaction value. (refer to Rule 5)
(2) Sale at the place of removal, price is excluding taxes, transport charges collected separately-	Rule 5 is not applicable, transaction value is applicable. Profit on transport if any need not be added to the transaction value.
(3) Where the manufacturer follows equalised freight system.	The profit made on transportation need not be added to the value. That means such profit is not taxable.

RULE 6 – PRICE NOT SOLE CONSIDERATION

Apply this rule under the following conditions:

- There is a sale at the place of removal, but the consideration received is not the total consideration. It means, if the same goods are sold in the open market, they would fetch more money.
- This rule provides for adding to the transaction value the money value of any additional consideration flowing directly or indirectly from the buyer to the assessee.
- Additional consideration is arrived at by adding all other considerations to the transaction value that flowed directly or indirectly from the buyer to the assessee.
- Additional consideration is the difference in prices between the price at which goods actually sold and the offer price (CCE. V. IFGL Refractories Ltd. – 2005 (186) E.L.T. 529 (S.C.)

The value of the items given is added to the consideration to make it the transaction value i.e.

- Value of materials, components, parts and similar items relatable to such goods.
- Value of tools, dies, moulds, drawings, blue prints, technical maps and charts and similar items used in the production of such goods.

- Value of material consumed, including packaging materials in the production of such goods.
- Value of engineering, development, art work, design work and plans and sketches.
- No notional interest shall be added to the value for the advance amount received from the buyer unless the Central Excise Officer has evidence to effect that the advance received has influenced the fixation of the price of the goods by way of charging the lesser price.

Example:

1. *X an assessee, sells his goods to Y against full advance payment at ₹100 per piece. However, X also sells such goods to Z without any advance payment at the same price of ₹100 per piece.*

Solution: No notional interest on the advance received by X is includable in the transactional value.

2. *A, an assessee, manufactures and supplies certain goods as per design and specification furnished by B at a price of ₹ 10 lakhs. A takes 50% of the price as advance against these goods and there is no sale of such goods to any other buyer.*

There is no evidence available with the Central Excise Officer that the notional interest on such advance has resulted in lowering of the prices. Thus, no notional interest on the advance received shall be added to the transaction value.

Important Points

- *a subsidy received from the Government (and not from buyer of the goods) is not addable in value – C.C.E. v. Kashmir Handloom Industries – 2005 (190) E.L.T. A43 (S.C.); C.C.E. V. Mazagaon Dock Ltd. – 2005 (187) E.L.T. 3 (S.C.)*
- *Burden of proof will be on the department.*
- *Penetration price: Recently, the Apex Court (S.C) gave a ruling that if a price below cost is charged to have penetration into the market with a view to make profits in future; the price is not sole consideration. [Fiat India Pvt Ltd, 2012, S.C]*

RULE 7 – WHEN GOODS ARE SOLD FROM SALES DEPOT, OR ANY OTHER PLACE

When there is removal of goods from factory as stock transfer, to the sales depot, place of consignment agent or any other place, the value of the goods will be the price prevailing at the depot, etc. on the date of removal from the factory.

As per the rules, assessment is to be made at the time of removal of goods from the factory or warehouse as the case may be. Dutiability and rate of duty are ascertained on the date of removal. As assessment is necessary on the date of removal, the price prevailing at the place of sale on the date of removal is taken.

- For instance, the goods are cleared from the factory today for sale to be made from the depot, the duty is assessed on the basis of the price prevailing at the depot today. It means it is the price at which actual transaction took place today at the depot.
- If there is no sale and the price is not available at the depot on the date of removal from the factory/warehouse, then the price at the depot on the date (preceding) nearest to the date of removal shall be taken.
- If different quantities are sold at different rates, then normal transaction value shall be applied. Normal transaction value as per Rule 2(b) means 'price of the aggregate greatest quantity' If the above scheme can not be applied then rule 11 shall be applied.

Excise duty is chargeable on the price at the place of sale. Since the place of sale branch/ depot in case of stock transfer, all expenses upto the sales depot shall be included for the purpose of value.

RULE 8 – WHEN GOODS ARE NOT SOLD BUT CAPTIVELY CONSUMED:

When the goods manufactured are not sold but are reused in the factory for the manufacture of other articles, the value for the purpose of excise shall be 110% of the cost of production. Captive consumption means self consumption. As a measure of simplification, the goods which are captively consumed are to be now valued on cost construction method as per the Cost Accounting Standards (CAS 2,3,4) only as there have been disputes in adopting values of comparable goods..

Example: If the cost of production based upon general principles of costing of a commodity is ₹10,000 per unit, the assessable value of the goods shall be ₹11,000 per unit.

The Board in its Circular No. 692/8/2003, dated 13-02-2003 has clarified that for calculating the cost of production for goods captively consumed, the CAS-4 issued by the Institute of Cost Accountants of India should be strictly followed.

As per CAS-4, treatment of the following elements of cost shall be as follows:

- *Deduct/ exclude vattable taxes from the cost of material. Vattable taxes include excise duty and VAT paid on local purchases.*
- *Exclude realizable scrap value from the cost.*
- *Do not consider selling and distribution overheads for finding out cost of production*
- *Add quality control costs*
- *Add research and development charges.*
- *Add amortized cost of capital goods (depreciation) used in production.*
- *Do not consider abnormal losses/ costs*
- *Do not consider nonrecurring expenses*

Note: advertisement and insurance charges are not includable in cost of production [Cadbury India Ltd. (S.C)]

RULE 9 - SALE TO RELATED PERSON OTHER THAN INTER-CONNECTED UNDERTAKING:

This rule covers those situations where goods are sold to or through related persons other than the Inter-Connected undertakings. In such a case, the value shall be the normal transaction value at which these are sold by the related person to unrelated persons. Normal transaction value means price of the greatest aggregate quantity. If the goods are not sold by the related person, but consumed captively, the value shall be determined as per Rule 8. i.e. 110% of cost of production.

RULE 10 – SALE TO / THROUGH INTER-CONNECTED UNDERTAKINGS (AND RELATED):

If the inter-connected undertakings also happen to be the related persons under the remaining clauses or they happened to be holding and subsidiary companies, then Transaction Value shall be determined as per Rule 9. In any other case (i.e. the buyer and the seller are merely the inter-connected undertakings), the value shall be determined under Section 4(1)(a), as if they are not related persons at all.

Mere interconnection doesn't affect the valuation. If the Inter-connected Undertakings are otherwise related under other clauses, then only Rule 9 is applied.

The following table will clarify the applicability of Rules 9 and 10:

Situation	Rule Applicable
If the related person is relative, distributor cum relative, mutually interested, holding or subsidiary of assessee.	Apply Rule 9
All other cases including an interconnected undertaking which is not a holding/ subsidiary of assessee.	Apply Rule 10 that means transaction value can be applied by ignoring the relation.

Rule 10A: Valuation under Job Work:

Earlier there was no specific rule for valuation of goods by job worker. Hence Rule 11 was applied by using the mechanism given under Rule 6. This Rule 10A came into effect from 1-4- 2007.

According to this rule, where goods are manufactured by job worker on behalf of a person (commonly known as principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, *as against the earlier practice where the value is taken as cost of inputs plus the job charges.*

- (a) The price charged by the principal manufacturer at the time of removal of goods from the premises of the job worker shall be taken for valuation.
- (b) Such price shall be sole consideration and the principal manufacturer and the buyer shall not be related persons.
- (c) If the price is not sole consideration, follow the mechanism given under Rule 6 and if the transaction is related persons transaction, follow rule 9.

If the goods are removed at a place other than the place of job worker, then apply normal transaction value of that place of removal as is done under Rule 7.

Circular No. 902/22/ 2009: Rule 10A

It has been brought to the notice of the Board that some manufacturers of Motor Vehicles are getting complete Motor Vehicles manufactured by sending the Chassis of the Motor Vehicles to independent body builders for building the body as per the design/specification of the manufacturer. The practice followed is that the Chassis is transferred to the Body builder on payment of appropriate Central Excise duty on stock transfer basis **and is not sold to them**. The body builder avails the Cenvat Credit of the duty paid on the chassis and clears the same on payment of duty to the Depot/Sales Office/Distributer of the Motor Vehicle manufacturer. The duty is discharged by the body builder on the assessable value comprising the value of Chassis and the job charges. The Depot/Sales office of the MV manufacturer sells the vehicles at a higher price than the price on which duty has been paid. Similar practice may be prevailing in respect of other commodities also.

RULE 11 – RESIDUAL METHOD/METHOD OF REASONABLE MEANS

When the value cannot be determined by any of the valuation rules, it shall be determined using reasonable means consistent with the principles and general provisions of these rules and Section 4(1).

CASE STUDIES RELATING TO VALUATION

1. PEPSI FOODS LTD. 2011 (S.C): Related Person Transactions

PEPSI is a manufacturer of edible chips. It sells through its related person Frito Lay- India. Frito Lay- India sold the products through its sales depot.

Issue: Whether the freight charges from Frito Lay-India to its sales depot are deductible from the depot price.

Held: No

Reason: The price charged by related person is acceptable under Rule 9 of Valuation Rules when the goods are sold at the place of the related persons. If the sale is from other place, the price at that other place shall be taken. Hence the freight charges upto the depot are not deductible.

2. ELECTRONICS & CONTROLS POWER SYSTEMS (P) LTD-2011 (S.C): Valuation of Bought Out Parts

Issue: Whether bought out batteries supplied with UPSS (Uninterrupted Power Supply System) as optional item is to be added to the value of the UPSS supplied.

Held: YES.

Why battery is an essential part of UPSS even though it can function without the battery.

Note: It is not necessary that the value of a bought out accessory should be included in the value of the manufactured goods supplied. The value of an article is to be added only if it is a component of the main article and not to be added if it serves only as an accessory.

The difference is – a component is an important part of the article whereas an accessory is nonessential for the product.

3. ROYAL ENFIELD, 2011, 13 SCC 135 (S.C)

Packing charges incurred in carrying motor cycles from factory to depot are includible even though they are charged separately from the customer as they are essential in putting the goods in marketable condition.

Annexure

THE CENTRAL EXCISE VALUATION (DETERMINATION OF PRICE OF EXCISABLE GOODS) RULES, 2000

Notification No. 45/2000 - Central Excise (N.T.)

Dated 30th June, 2000 as amended

G.S.R. (E) — In exercise of the powers conferred by Section 37 of the Central Excise Act, 1944 (1 of 1944) and in supersession of the Central Excise (Valuation) Rules, 1975 except as respect things done or omitted to be done before such supersession, the Central Government hereby makes the following rules, namely:

1. (1) these rules may be called the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000.
- (2) They shall come into force on and from the 1st day of July, 2000.

CHAPTER I PRELIMINARY

2. In these rules, unless the context otherwise requires:
 - (a) "Act" means the Central Excise Act, 1944 (1 of 1944);
 - (b) "normal transaction value" means the transaction value at which the greatest aggregate quantity of goods are sold;

- (c) "value" means the value referred to in Section 4 of the Act;
- (d) words and expressions used in these rules and not defined but defined in the Act shall have the meanings respectively assigned to them in the Act.

CHAPTER II

DETERMINATION OF VALUE

3. The value of any excisable goods shall, for the purposes of clause (b) of sub-section (1) of Section 4 of the Act, be determined in accordance with these rules.
4. The value of the excisable goods shall be based on the value of such goods sold by the assessee for delivery at any other time nearest to the time of the removal of goods under assessment, subject, if necessary, to such adjustment on account of the difference in the dates of delivery of such goods and of the excisable goods under assessment, as may appear reasonable.
5. Where any excisable goods are sold in the circumstances specified in Clause (a) of Sub-section (1) of Section 4 of the Act except the circumstance in which the excisable goods are sold for delivery at a place other than the place of removal, then the value of such excisable goods shall be deemed to be the transaction value, excluding the actual cost of transportation from the place of removal upto the place of delivery of such excisable goods provided the cost of transportation is charged to the buyer in addition to the price for the goods and shown separately in the invoice for such excisable goods.
6. Where the excisable goods are sold in the circumstances specified in Clause (a) of Sub-section (1) of Section 4 of the Act except the circumstance where the price is not the sole consideration for sale, the value of such goods shall be deemed to be the aggregate of such transaction value and the amount of money value of any additional consideration flowing directly or indirectly from the buyer to the assessee.

Explanation : For removal of doubts, it is hereby clarified that the value, apportioned as appropriate, of the following goods and services, whether supplied directly or indirectly by the buyer free of charge or at reduced cost for use in connection with the production and sale of such goods, to the extent that such value has not been included in the price actually paid or payable, shall be treated to be the amount of money value of additional consideration flowing directly or indirectly from the buyer to the assessee in relation to sale of the goods being valued and aggregated accordingly, namely:

- (i) value of materials, components, parts and similar items relatable to such goods;
- (ii) value of tools, dies, moulds, drawings, blue prints, technical maps and charts and similar items used in the production of such goods;
- (iii) value of material consumed, including packaging materials, in the production of such goods;
- (iv) value of engineering, development, art work, design work and plans and sketches undertaken elsewhere than in the factory of production and necessary for the production of such goods.

Explanation 2. - Where an assessee receives any advance payment from the buyer against delivery of any excisable goods, no notional interest on such advance shall be added to the value unless the Central Excise Officer has evidence to the effect that the advance received has influenced the fixation of the price of the goods by way of charging a lesser price from or by offering a special discount to the buyer who has made the advance deposit.

Illustration 1. - X, an assessee, sells his goods to Y against full advance payment at ₹ 100 per piece. However, X also sells such goods to Z without any advance payment at the same price of ₹ 100 per piece. No notional interest on the advance received by X is includable in the transaction value.

Illustration 2. - A, an assessee, manufactures and supplies certain goods as per design and specification furnished by B at a price of ₹ 10 lakhs A takes 50% of the price as advance against these goods and there is no sale of such goods to any other buyer. There is no evidence available with the Central Excise Officer that the notional interest on such advance has resulted in lowering of the prices. Thus, no notional interest on the advance received shall be added to the transaction value.]

7. Where the excisable goods are not sold by the assessee at the time and place of removal but are transferred to a depot, premises of a consignment agent or any other place or premises (hereinafter referred to as "such other place") from where the excisable goods are to be sold after their clearance from the place of removal and where the assessee and the buyer of the said goods are not related and the price is the sold consideration for the sale, the value shall be the normal transaction value of such goods sold from such other place at or about the same time and, where such goods are not sold at or about the same time, at the time nearest to the time of removal of goods under assessment.
8. Where the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value shall be one hundred and ten per cent of the cost of production or manufacture of such goods.
9. When the assessee so arranges that the excisable goods are not sold by an assessee except to or through a person who is related in the manner specified in either of sub-clause (ii), (iii) or (iv) of Clause (b) of Sub-section (3) of Section 4 of the Act, the value of the goods shall be the normal transaction value at which these are sold by the related person at the time of removal, to buyers (not being related person); or where such goods are not sold to such buyers, to buyers (being related person), who sells such goods in retail :

Provided that in a case where the related person does not sell the goods but uses or consumes such goods in the production or manufacture of articles, the value shall be determined in the manner specified in Rule 8.

10. When the assessee so arranges that the excisable goods are not sold by him except to or through an inter-connected undertaking, the value of goods shall be determined in the following manner, namely:
 - (a) If the undertakings are so connected that they are also related in terms of Sub-clause (ii) or (iii) or (iv) of Clause (b) of Sub-section (3) of Section 4 of the Act or the buyer is a holding company or subsidiary company of the assessee, then the value shall be determined in the manner prescribed in Rule 9.

Explanation : In this clause "holding company" and "subsidiary company" shall have the same meanings as in the Companies Act, 1956 (1 of 1956).

 - (b) In any other case, the value shall be determined as if they are not related persons for the purpose of Sub-section (1) of Section 4.
- 10A. Where the excisable goods are produced or manufactured by a job-worker, on behalf of a person (hereinafter referred to as principal manufacturer), then, -
 - (i) in a case where the goods are sold by the principal manufacturer for delivery at the time of removal

of goods from the factory of job-worker, where the principal manufacturer and the buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the transaction value of the said goods sold by the principal manufacturer;

- (ii) in a case where the goods are not sold by the principal manufacturer at the time of removal of goods from the factory of the job-worker, but are transferred to some other place from where the said goods are to be sold after their clearance from the factory of job-worker and where the principal manufacturer and buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the normal transaction value of such goods sold from such other place at or about the same time and, where such goods are not sold at or about the same time, at the time nearest to the time of removal of said goods from the factory of job-worker;
- (iii) in a case not covered under clause (i) or (ii), the provisions of foregoing rules, wherever applicable, shall *mutatis mutandis* apply for determination of the value of the excisable goods :

Provided that the cost of transportation, if any, from the premises, wherefrom the goods are sold, to the place of delivery shall not be included in the value of excisable goods.

Explanation. - For the purposes of this rule, job-worker means a person engaged in the manufacture or production of goods on behalf of a principal manufacturer, from any inputs or goods supplied by the said principal manufacturer or by any other person authorised by him.

11. If the value of any excisable goods cannot be determined under the foregoing rules, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules and Sub-section (1) of Section 4 of the Act.

(T.R. Rustagi)

Joint Secretary to the Government of India

F.No. 354/81/2000-TRU

MEANING OF INTER CONNECTED UNDERTAKINGS

"Inter-connected undertakings" means two or more undertakings which are inter-connected with each other in any of the following manners, namely:—

- (A) if one owns or controls the other;
- (B) where the undertakings are owned by firms, if such firms have one or more common partners;
- (C) where the undertakings are owned by bodies corporate,—
 - (I) if one body corporate manages the other body corporate; or
 - (II) if one body corporate is a subsidiary of the other body corporate; or
 - (III) if the bodies corporate are under the same management; or
 - (IV) if one body corporate exercises control over the other body corporate in any other manner;
- (D) where one undertaking is owned by a body corporate and the other is owned by a firm, if one or more partners of the firm,—
 - (I) hold, directly or indirectly, not less than fifty per cent. of the shares, whether preference or equity, of the body corporate; or
 - (II) exercise control, directly or indirectly, whether as director or otherwise, over the body corporate;
- (E) if one is owned by a body corporate and the other is owned by a firm having bodies corporate as its partners, if such bodies corporate are under the same management;

- (F) if the undertakings are owned or controlled by the same person or by the same group;
- (G) if one is connected with the other either directly or through any number of undertakings which are inter-connected undertakings within the meaning of one or more of the foregoing sub clauses.

Explanation I.— For the purposes of this clause, two bodies corporate shall be deemed to be under the same management,—

- (i) if one such body corporate exercises control over the other or both are under the control of the same group or any of the constituents of the same group; or
- (ii) if the managing director or manager of one such body corporate is the managing director or manager of the other; or
- (iii) if one such body corporate holds not less than one-fourth of the equity shares in the other or controls the composition of not less than one-fourth of the total membership of the Board of directors of the other; or
- (iv) if one or more directors of one such body corporate constitute, or at any time within a period of six months immediately preceding the day when the question arises as to whether such bodies corporate are under the same management, constituted (whether independently or together with relatives of such directors or employees of the first mentioned body corporate) one-fourth of the directors of the other; or
- (v) if the same individual or individuals belonging to a group, while holding (whether by themselves or together with their relatives) not less than one-fourth of the equity shares in one such body corporate also hold (whether by themselves or together with their relatives) not less than one-fourth of the equity shares in the other; or
- (vi) if the same body corporate or bodies corporate belonging to a group, holding, whether independently or along with its or their subsidiary or subsidiaries, not less than one-fourth of the equity shares in one body corporate, also hold not less than one-fourth of the equity shares in the other; or
- (vii) if not less than one-fourth of the total voting power in relation to each of the two bodies corporate is exercised or controlled by the same individual (whether independently or together with his relatives) or the same body corporate (whether independently or together with its subsidiaries); or
- (viii) if not less than one-fourth of the total voting power in relation to each of the two bodies corporate is exercised or controlled by the same individuals belonging to a group or by the same bodies corporate belonging to a group, or jointly by such individual or individuals and one or more of such bodies corporate; or
- (ix) if the directors of one such body corporate are accustomed to act in accordance with the directions or instructions of one or more of the directors of the other, or if the directors of both the bodies corporate are accustomed to act in accordance with the directions or instructions of an individual, whether belonging to a group or not.

Explanation II.— If a group exercises control over a body corporate, that body corporate and every other body corporate, which is a constituent of, or controlled by, the group shall be deemed to be under the same management.

Explanation III.— If two or more bodies corporate under the same management hold, in the aggregate, not less than one-fourth equity share capital in any other body corporate, such other

body corporate shall be deemed to be under the same management as the first mentioned bodies corporate.

Explanation IV.— In determining whether or not two or more bodies corporate are under the same management, the shares held by financial institutions in such bodies corporate shall not be taken into account.

Illustration

Undertaking B is inter-connected with undertaking A and undertaking C is inter-connected with undertaking B. Undertaking C is inter-connected with undertaking A; if undertaking D is inter-connected with undertaking C, undertaking D will be inter-connected with undertaking B and consequently with undertaking A; and so on.

Explanation V- For the purposes of this clause, "group" means a group of two or more individuals, associations of individuals, firms, trusts, trustees or bodies corporate (excluding financial institutions), or any combination thereof, which exercises, or is established to be in a position to exercise, control, directly or indirectly, over anybody corporate, firm or trust; or associated persons.

Explanation VI- For the purposes of this clause,

- (I) group of persons who are able, directly or indirectly, to control the policy of a body corporate, firm or trust, without having a controlling interest in that body corporate, firm or trust, shall also be deemed to be in a position to exercise control over it;
- (II) "associated persons"—
 - (a) in relation to a director of a body corporate, means—
 - (i) a relative of such director, and includes a firm in which such director or his relative is a partner;
 - (ii) any trust of which any such director or his relative is a trustee;
 - (iii) any company of which such director, whether independently or together with his relatives, constitutes one-fourth of its Board of directors;
 - (iv) any other body corporate, at any general meeting of which not less than one-fourth of the total number of directors of such other body corporate are appointed or controlled by the director of the first mentioned body corporate or his relative, whether acting singly or jointly;
 - (b) in relation to the partner of a firm, means a relative of such partner and includes any other partner of such firm; and
 - (c) in relation to the trustee of a trust, means any other trustee of such trust;
- (III) where any person is an associated person in relation to another, the latter shall also be deemed to be an associated person in relation to the former;

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What are the methods of valuation under Excise? Which method is used mostly?
2. What is the scheme of valuation under section 4A?
3. It is admitted that in regard to certainty of taxation and convenience to the assessee as well as the revenue authority, specific rates of duty are preferable to ad valorem rates of duty. Still, the Excise Department has shown a pronounced preference for ad valorem rates. Why?

4. Explain the 'Concept of Transaction Value' as defined in Section 4(3)(d) of the Central Excise Act, 1944.
5. MRP scheme under Section 4A is governed mostly by Legal Metrology Act, 2009- comment
6. What are the conditions to be satisfied under Section 4(1) (a) to apply sale price directly without the use of Valuation Rules?
7. Who is a related person? How are the transactions with related persons valued?
8. Explain the following with reference to the determination of 'Assessable Value' under Section 4 of the Central Excise Act.
 - "Assessee".
 - "Place of removal".
 - "Normal transaction value"
9. What is the relevance of enactment of Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 in determination of 'assessable value'?
10. How are the goods manufactured by a job worker are valued?
11. Calculate the assessable value from the following information:
 Total production 3000 units; sold 750 units @ 200 per unit and 950 units @ 190 and 150 units were distributed as free samples. The prices above are excluding taxes.
12. Determine the transaction value and excise duty from the following:
 Total price charged at the sales depot is 200,000 which includes the following; VAT ₹ 10,000 ; octroi 2,000; insurance from factory to depot ₹ 2,000; freight from factory to depot ₹ 8,000 ; excise duty is 12% and cess as applicable.
13. Contracted price for delivery at buyer's premises: ₹ 8,00,000. which included the following:
 (i). cost of drawings and design ₹ 4,000; (ii). Cost of primary packing ₹ 8,000 ; (iii). Cost of packing at buyer's request ₹ 10,000; sales tax 28,000 and excise duty 12.36%; (iv). Octroi ₹ 2500; freight and insurance charges paid from factory to warehouse ₹ 20,000; (v). actual freight and insurance from place of removal(warehouse) to buyer's premises ₹ 45,600
14. Tej Ltd. cleared 5 lakh biscuit packets each bearing a retail price of ₹20. Due to delay in transportation, the quality was affected and the goods had to be sold in public auction at Rs 10 per pack. The goods are notified under section 4A and Abatement rate is 35%. Find out the assessable value.
15. Goods notified under section 4A were cleared from factory with an MRP of ₹ 100 to Branch. After receiving the goods at the branch, the packet was split into two and each pack was relabeled with an MRP of Rs 60. How are the goods assessed?
16. State whether the assessment is necessary at the branch also?
17. An assessee sells goods to A Ltd. for ₹100,000 on 15th December, 2012 The buyer is a 'related person. On that date, the net price (excluding excise duty) of related person to an unrelated buyer was ₹1,10,000. What will be the assessable Value' in each of the following cases
 - (a) The related person sells the goods to an unrelated buyer on 5th February, 2013 at ₹120,000, exclusive of excise duty.

- (b) The related person sells the goods to unrelated buyer on 10th February, 2013 at ₹ 1,25,000, exclusive of excise duty.
 - (c) The buyer is an 'inter connected undertaking' in relation to manufacturer (assessee). However, the buyer is not a holding or subsidiary of the assessee. Buyer and seller do not have interest in each other.

SUGGESTED READINGS

- (1) Indirect Taxes—Law & Practice – *V.S Datey, Taxmann*
 - (2) Central Excise Law Manual – *R.K. Jain, Centax Publications, New Delhi*
 - (3) Excise Law Times – *Centax Publication, New Delhi*

CENTRAL EXCISE LAW

PART IV: REGISTRATION, ASSESSMENT, PAYMENT, CLEARANCE AND EXEMPTION OF DUTIES

At the end of this part, the students will

- Familiar with the registration procedure
- Have the understanding of the assessment procedures
- Be fully acquaint with the payment procedure, filing of return procedures
- Have the understanding of the exemption provisions

INTRODUCTION

Central excise is procedure oriented. The procedures are so important that even a slight violation will lead to serious consequences, such as confiscation, penalty and prosecution. Under the self assessment regime, a definite system has been laid down by Government. The procedures under excise can be classified as general and special. General procedures were laid down under CER, 2002 which are routine in nature. In this chapter, we study the procedures involved in registration, storage, removal, payment of duty etc.

Before moving to the procedural aspects let's take an overview of the Central Excise Rules, 2002:

CENTRAL EXCISE RULES, 2002 AT A GLANCE

Rule 1	Short title, extent and commencement
Rule 2	Definitions
Rule 3	Appointment and jurisdiction of Central Excise Officers
Rule 4	Duty payable on removal
Rule 5	Date for determination of duty and Tariff valuation
Rule 6	Assessment of duty
Rule 7	Provisional Assessment
Rule 8	Manner of payment of duty
Rule 9	Registration
Rule 10	Daily stock Account
Rule 11	Goods to be removed on invoice
Rule 12	Filing of Return
Rule 12AA	Job work in articles of Jewellery
Rule 12BB	Procedure and facilities for Large tax payer.
Rule 12CCC	Power to impose restrictions in certain types of cases
Rule 15	Special Procedure for payment of duty

Rule 16	Credit of duty on goods brought to factory
Rule 16A	Removal of goods for Job work
Rule 16B	Special procedure for removal of semi-finished goods for certain purposes
Rule 16C	Special procedure for removal of excisable goods for carrying out certain processes
Rule 17	Removal of goods by a 100% Export Oriented Unit for Domestic Tariff Area
Rule 18	Rebate of duty
Rule 19	Export without payment of duty
Rule 20	Warehousing provisions
Rule 21	Remission of duty
Rule 22	Access to registered premises
Rule 23	Power to stop and search
Rule 24	Power to detain/ seize goods
Rule 25	Confiscation and Penalty
Rule 26	Penalty for certain cases
Rule 27	General Penalty
Rule 28	Confiscation, Property to Vest in Central Govt.
Rule 29	Disposal of confiscated goods
Rule 30	Storage charges in respect of goods confiscated and redeemed
Rule 31	Power to issue supplementary instructions
Rule 32	Omitted
Rule 33	Transitional provision

Note: The Rules which are not discussed under this chapter are discussed in other chapters.

REGISTRATION

For the administration of the Central Excise Act, 1944 and the Central Excise Rules, 2002 manufacturers' of excisable goods or any person who deals with excisable goods, with some exceptions, are required to get the premises registered with the Central Excise Department before commencing business.

PERSONS REQUIRING REGISTRATION

In accordance with Rule 9 of the said Rules and Notifications issued under rules 18 and 19 of the said Rules, as the case may be, the following category of persons are required to register with jurisdictional Central Excise Officer in division office having jurisdiction over his place of business/factory:

1. Every manufacturer of excisable goods (including Central/State Government undertakings or undertakings owned or controlled by autonomous corporations) on which excise duty is leviable .
2. Persons who desire to issue CENVATABLE invoices under the provisions of the CENVAT Credit Rules, 2001.

3. Persons holding private warehouses.
4. Persons who obtain excisable goods for availing end-use based exemption notification or an importer who issues an invoice on which CENVAT credit can be taken.
5. Exporters manufacturing or processing export goods by using duty paid inputs and intending to claim rebate of such duty or by using inputs received without payment of duty and exporting the finished export goods.

EXEMPTION FROM REGISTRATION

The Central Board of Excise and Customs (CBEC), by Notification No. 36/2001-CE (NT) dt.26.6.2001, has exempted specified categories of persons/premises from obtaining registration, as follows:

- Persons who manufacture the excisable goods, which are chargeable to nil rate of excise duty or are fully exempt from duty by a notification.
- Small scale units availing the slab exemption based on value of clearances under a notification. However, such units will be required to give a declaration once the value of their clearances touches ₹90 lakhs.
- In respect of ready-made garments and articles of jewellery, the job-worker need not get registered. The principal manufacturer has to discharge the duty liability.
- Persons manufacturing excisable goods by following the warehousing procedure under the Customs Act, 1962 subject to the following conditions:
 - the said excisable goods and any intermediary or by-product including the waste and refuse arising during the process of manufacture of the said goods under the Customs Bond are either destroyed or exported out of the country to the satisfaction of the Assistant Commissioner of Customs or the Deputy Commissioner of Customs, in-charge of the Customs Bonded Warehouse;
 - the manufacturer shall file a declaration in the specified form annexed hereto in triplicate for claiming exemption under this notification;
 - no drawback or rebate of duty of excise paid on the raw materials or components used in the manufacture of the said goods, shall be admissible.
- The person who carries on wholesale trade or deals in excisable goods (except first and second stage dealer, as defined in Cenvat Credit Rules, 2004).
- A Hundred per cent Export Oriented Undertaking, or a unit in Free Trade Zone or Special Economic Zone licensed or appointed, as the case may be, under the provisions of the Customs Act, 1962.
- Persons who use excisable goods for any purpose other than for processing or manufacture of goods availing benefit of concessional duty exemption notification.
- Where a godown or retail outlet of a Duty Free Shop is appointed or licensed under the provision of Section 57 or 58 of the Customs Act, 1962. (52 of 1962)

PROCEDURE FOR REGISTRATION

1. Application for Registration

Under authority of Section 6 of the Central Excise Act, 1944 read with rule 9 of the said Rules, the CBEC has prescribed the format for Application as well as Registration Certificate. The application has to be made to the jurisdictional Central Excise Officer.

2. The application for registration should be signed by:

- The applicant or by his authorised agent having general power of attorney. The Range Officer shall have power to call the original documents to verify 'power of attorney'. Such document shall not be retained by the Range Officer but be returned immediately after verification.
- In case of unregistered partnership firms, by all partners.
- In case of registered partnerships, by the managing partner or other partner so authorised in the Partnership Deed.

When a manufacturer who is exempt from the registration is required to file a declaration, the same will be filed with the Assistant Commissioner of the jurisdictional Central Excise Division.

3. Separate Registration

Separate registration is required in respect of separate premises except in cases where two or more premises are actually part of the same factory (where processes are interlinked), but are segregated by public road, canal or railway-line. The fact that the two premises are part of the same factory will be decided by the Commissioner of Central Excise based on factors, such as:

- Interlinked process – product manufactured/produced in one premise are substantially used in other premises for manufacture of final products.
- Large number of raw materials are common and received/proposed to be received commonly for both/all the premises
- Common electricity supplies.
- There is common labour /work force
- Common administration/ works management.
- Common sales tax registration and assessment
- Common Income Tax assessment
- Any other factor as may be indicative of inter-linkage of the manufacturing processes. This is neither an exhaustive list of indicators nor each indicator is necessarily in each case. The Commissioner has to decide the issued from case to case.

Separate Registration is required for each depot, godown etc. in respect of persons issuing Cenvat invoices. However, in the case liquid and gaseous products, availability of godown should not be insisted upon.

4. Registration Certificate

Registration Certificate may be granted to minors provided they have legal guardians i.e. natural guardians or guardians appointed by the Court, as the case may be, to conduct business on their behalf.

5. Filing of Declaration in lieu of registration

The manufacturers who are exempted from the operation of Rule 9 by virtue of Notification no. 36/2001-Central Excise (NT) dt.26/6/2001 have to file a declaration with the Assistant Commissioner of the respective Divisions. Such declarations received from the assessee will have to be filed separately, tariff head-wise in the Divisional office. The details should be entered in the register to be maintained in the Divisional office in the enclosed proforma. Genuine delay in filing the required declaration need not be viewed seriously and the assessee may be allowed to enjoy the exemption from the operation of Rule 9 as well as from the payment of duty provided the conditions stipulated in the respective exemption Notifications have been duly fulfilled.

6. Procedure of Issue of Registration Certificate

Under the section 6 of the Central Excise Act, 1944 read with rule 9 of the said Rules, the CBEC, by

notification, has specified the format for Application as well as Registration Certificate (Annexure 2 and 3, respectively). The format of application is common to manufacturers, private warehouse holders, and registered dealers issuing CENVATABLE invoice and persons who obtain goods by availing end-use based exemptions, including manufacturers or processors of export goods.

In the application for Registration, the applicant has to submit ground plan. Under the Central Excise Rules, 2002, there is no stipulation of any specified marked area for storing the finished goods (traditionally called the 'bonded store room'). Thus there is no need for marking such area in the ground plan. The only verification that the jurisdictional officers should conduct that the premises mentioned in the application for registration, are genuine and are intended for the purposes for which the application has been made. Assessee, however, shall be responsible for proper storage and accountal of goods manufactured in his factory at any point of time.

The verification shall be made by the Inspector or Superintendent of Central Excise having jurisdiction over the premises (Range Officer) in respect of which the applicant has sought registration, within 5 working days of the receipt of application. As per the rules/notification, the registration certificate shall be issued within 7 working days. The Range Officer (Superintendent) either himself or through the Sector Officer (Inspector) shall verify whether the declared address and operations (intended) are genuine and the declarations made in the application are correct. If found in order, he will endorse the correctness of the same and append his dated signature on the office copies of the Registration application and the copy of the application with the registrant. If any deviations or variations are noticed during the verification, the same should be got corrected. Any major discrepancy, such as fake address, non-existence of any factory etc. shall be reported in writing to the Divisional Officer within 3 working days and the Range Officer shall initiate action to safeguard revenue.

7. Issue of Registration Certificate.

All Registrations of each type should be numbered in a single series for the Range as a whole, commencing with serial no. 1 for each calendar year. The issuing authority should make every effort to complete all formalities and grant the Registration Certificate within 7 days of receipt of application in his office. Every Registration Certificate granted / issued by the registering authority shall be under his signature. He should also countersign the ground plan accompanying the Registration Certificate. The Registration Certificate and the duplicate copy of the plan should be returned to the registered person who shall exhibit his Registration Certificate or a certified copy thereof in a conspicuous part of the registered premises. The Registering authority in a permanent file shall keep the application as well as the ground plan. In case of partnership firms, the Registration Certificate which is granted in the name of the said firm [which is registered or not under the Partnership Act] shall contain the names of all the partners. The Registration Certificate or a certified copy thereof is required to be exhibited in a conspicuous part of the registered premises.

8. Period of Validity of Registration

Once Registration Certificate is granted, it has a permanent status unless it is suspended or revoked by the appropriate authority in accordance with law or is surrendered by the person or company concerned. If the person who applies for Registration with the department is an individual, then the Certificate would cease to be valid in the event of the death of the said individual. Any other person(s) who wish(es) to continue with the operations for which the deceased person was registered, he would then have to apply afresh. (See notification no. 35/2001-Central Excise (N.T.) dated 26th June, 2001.). In the case of limited company, death of a director would not affect the status of Registration, since Registration is issued to the body corporate recognizing the same as a legal person. In the case of partnership firms also normally no difficulty would arise with regard to succession, since the surviving partners will continue either in the same name or with the change of name the business. However, in the case of proprietary business when the proprietor dies, the successor in estate has to apply for a fresh Registration. Ordinarily fresh Registration would be issued to the

person who happens to be in the actual possession of the business. However, grant of fresh Registration to the successor in estate shall not be regarded that the Government has accepted the said person as the legal successor/heir to the deceased.

9. Surrender, Cancellation, Suspension or Revocation of Registration

Registration Certificate may be surrendered as per application in prescribed form in Notification No. 35/2001-CE (N.T.) dated 26.6.2001 [Annexure-4]. This is subject to compliance of the statutory obligations under the excise law, particularly the payment of all dues to the Government including the duty on finished excisable goods lying in the factory/warehouse. In case of mis-declaration regarding compliance, the surrender of registration shall not be valid. Registration Certificate may be cancelled by the Registering authority when the registered person voluntarily surrenders the Certificate due to closure of business. As per rule 17 of the said Rules Registration Certificate may be revoked or suspended by the Deputy/Assistant Commissioner of Central Excise, if the holder or any person under his employ has committed a breach of any condition of the Central Excises Act or the rules made thereunder or has been convicted of an offence under Section 161 read with Section 109 or Section 116 of the Indian Penal Code [45 of 1860].

Suspension or revocation of the Registration is a heavy punishment since it amounts to suspending or stopping the business and could result in grave damage to the person concerned. Hence this penalty should be resorted to only in cases where there is persistent misdemeanor involving serious loss of revenue.

The power to revoke or suspend the Registration is vested only with the Deputy/Assistant Commissioner. In case of suspension or revocation, the Range Officer should refer the matter to the Deputy/Assistant commissioner who will pass appropriate orders after affording a reasonable opportunity. Appeal against this order lies with the Commissioner[Appeals] and this should be specifically spelt out in the order -in-original of the Deputy/Assistant Commissioner(Preamble).

Procedure for registration under Automation of Central Excise and Service Tax (ACES)

New registrants are required to follow the below mentioned procedure

- Log on www.aces.gov.in and register accordingly by following the hyperlink “Click Here to Register with ACES”
- After entering the requisite details, click on ‘Submit’ button to get the response screen
- An acknowledgement is generated, which confirms that password has been delivered to the email address of the user which indicates that the user can now login as a normal user using his credentials
- Login with username and password
- Change password
- Click on “REG” tab and click on “Fill A - 1” from the drop down list
- Fill the form with desired details
- Proceed by clicking “Save & Continue”
- Duly filled A - 1 would be generated, giving the option to make any changes by way of “Modify” tab
- Print the duly filled/modified form
- Click on “Submit”
- Print the acknowledgement generated consequently
- Submit the printed form and printed acknowledgement along with requisite documents (self attested) to the excise authorities
- Obtain registration certificate

Note: Existing assessees are required to get themselves registered with ACES merely by filing a declaration with range officer and thereby obtaining TPIN and password from the department.

Documents required for registration (self attested copies)

- PAN card copy of the company/firm
- PAN card copy of authorized signatory
- Ground plan of factory (which should also provide description of boundaries of premises to be registered)
- List of directors/partners
- Memorandum and Articles of Association/Partnership deed
- General power of attorney (in case application is signed by authorized agent)

Apart from these, department may also require certain additional documents, some of which are mentioned hereunder:

- PAN card copy of directors/partners other than signatories
- Address proofs of the factory premises like:
- Copy of purchase agreement along with electricity bill, water bill etc., if factory is owned
- Copy of Leave and license agreement along with electricity bill, water bill etc., if factory is taken on lease
- ‘No objection certificate’ from the licensor and last paid rent receipt may also be required
- Residence proof of directors/partners
- Registration Certificate under any other laws, if any

ASSESSMENT

Assessment is quantification of the duty liability to be discharged by the assessee. Rule 2(b) of the Central Excise Rules, 2002 defines ‘assessment’ to include — self-assessment of duty made by the assessee and provisional assessment under Rule 7.

Accordingly assessment includes—

1. Self Assessment made by the Assessee,
2. Provisional Assessment under Rule 7.

1. SELF-ASSESSMENT

Under the self-assessment system introduced in 1996 for removals under Self Removal Procedure (SRP), the assessee himself is allowed to assess the duty liability and prepare a return on a monthly-basis (for SSI on quarterly-basis) and submit to the Central Excise Department. The Departmental officers are required to scrutinise the returns in the manner prescribed.

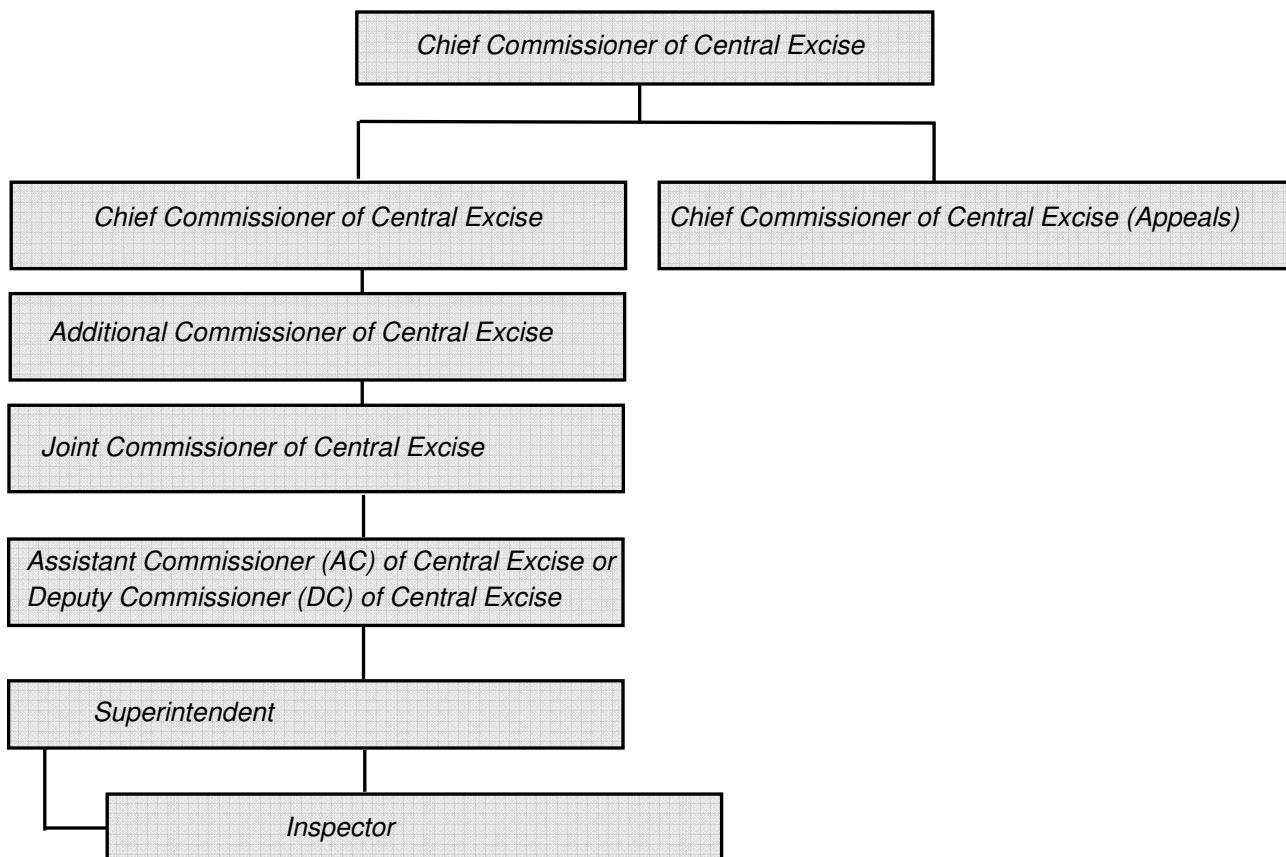
However, in case of cigarettes, the Superintendent or Inspector of Central Excise shall assess the duty payable before removal by the assessee.

The assessee is required to submit monthly return in ER-1 Form. This return has to be filed along with “Self

Assessment Memorandum" whereby, the assessee details that the particulars contained in ER-1 return are correctly stated, duty has been correctly assessed and paid as per the provisions of this Act. The return made shall be subject to scrutiny by the Departmental Officers, who may carry out surprise checks alongwith routine audit procedures.

As per section 2, "Central Excise Officer" means the Chief Commissioner of Central Excise, Commissioner of Central Excise, Commissioner of Central Excise (Appeals), Additional Commissioner of Central Excise, Joint Commissioner of Central Excise, Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise or any other officer of the Central Excise Department, or any person (including an officer of the State Government) invested by the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 (54 of 1963) with any of the powers of a Central Excise Officer under this Act.

A chart showing the Central Excise Officers



2. PROVISIONAL ASSESSMENT

Where the assessee is not in a position to determine either the value of the goods or the applicable rates of duty, in such circumstances, the remedy available to the assessee and the officer is the "Provisional Assessment". The provisional assessment is thus a temporary arrangement to keep the machinery in motion. The duty is thus assessed based on the available information and the goods are cleared after its payment. The final assessment is made on removal of reasons which necessitated the provisional assessment.

The provisions relating to the provisional assessment are laid under Rule 7 of the Central Excise Rules,

2002. Provisional Assessment can be requested by an assessee and department cannot suo moto order provisional assessment.

Reason for resorting to provisional assessment

Provisional assessment can be resorted to by an assessee under Rule 7(1) where he is unable to determine the value of excisable goods or rate of duty applicable thereto. In the aforesaid cases, assessee may request Assistant/Deputy Commissioner in writing giving reasons for payment of duty on provisional basis. After such request the Assistant/Deputy Commissioner may by order allow payment of duty on provisional basis and may also specify the rate or value at which the duty shall be paid on provisional basis.

Submission of security or surety

As per the provisions of Rule 7(2), the Assistant/Deputy Commissioner may allow an assessee to make payment of duty on provisional basis if he executes a B-2 bond with such surety or security in such amount as the Assistant/Deputy Commissioner of Central Excise deem fit, binding the assessee for payment of difference between the amount of duty as may be finally assessed and the amount of duty provisionally assessed.

Final Assessment

The Assistant/Deputy Commissioner shall pass order for final assessment under Rule 7(3) after getting relevant information within six months of date of communication of his order allowing provisional assessment. This period of six months can be extended by the Commissioner of Central Excise, on sufficient cause being shown and the reasons to be recorded in writing for a further period not exceeding six months and by the Chief Commissioner of Central Excise for such further period as he may deem fit.

Refund or payment of duty and interest thereon if any

In case of provisional assessment, final assessment will be done by Assistant/Deputy Commissioner. After final assessment if the duty payable is more, the difference will be paid by assessee. In case, the duty finally assessed is less; difference will be refunded [(Rules 7(4) and 7(5)]. Where the differential duty is found to be payable, interest at the rate specified by the Central Government by notification issued under Sections 11AA of the Act shall be payable by the assessee from first day of month succeeding the month for which such amount is determined till date of payment thereof. Thus, interest is payable only after assessment is finalised by Assistant/Deputy Commissioner of Central Excise.

In case differential amount is required to be refunded to the assessee, it shall be refunded with interest at the rate specified by the Central Government by notification (6%), issued under Section 11BB of the Act from the expiry of three months till the date of refund.

APPLICABILITY OF DOCTRINE OF UNJUST ENRICHMENT

Sub-rule (6) of Rule 7 lays that refund is subject to the provisions of "Unjust Enrichment" i.e. refund will be granted to manufacturer if he has not passed on incidence of duty to another person. As per this sub-rule, any amount of refund determined under Sub-rule (3) shall be credited to the Consumer Welfare Fund. However, it has been provided that the amount of refund, instead of being credited to the fund, be paid to the applicant, if such amount is relatable to:

- (a) the duty of excise paid by the manufacturer, if he had not passed on the incidence of such duty to any other person, or
- (b) the duty of excise borne by the buyer, if he had not passed on the incidence of such duty to any other person.

The following are the provisions of Provisional Assessment

1. *The provisional assessment shall be resorted where assessee is unable to determine the value and rate. Department cannot suo moto order provisional assessment.*
2. *Bond furnished for difference in duty finally assessed and provisionally assessed.*
3. *Order shall be passed by Assistant Commissioner/Deputy Commissioner.*
4. *Final assessment shall be passed within 6 month from the date of Provisional Assessment. However, this period may further be extended for 6 months by Commissioner of Central Excise and for any period by Commissioner of Central Excise.*
5. *Refund is subject to Doctrine of Unjust enrichment.*

PAYMENT OF EXCISE DUTIES

While duty liability is, no doubt, created by the act of manufacture, still, it should be impractical or unviable for the manufacturer to discharge the liability immediately, that is, at the very moment when the goods, are manufactured. Hence, the excise law has provided for postponement of payment of duty to a later point of time. *In Bombay Tyre International's case [1983 ELT 1896 (SC)],* the Supreme Court upheld the Legislature's choice of convenience in collecting the levy at the time of clearance of the excisable goods. Rule 4 and Rule 8 of Central Excise Rules, 2002 read together would indicate that duty has to be paid only at the time when the goods are removed from the premises of manufacturer or any other specified places.

1. THE RATE OF DUTY TO BE CHARGED ON GOODS

Section 3 of the Central Excise Act, 1944, which creates the charge and defines the nature of the charge of this tax, provides that the duties shall be paid at the rates set forth in the Schedules to the Central Excise Tariff Act, 1985. The rates at which excise duty is charged are thus prescribed in the Tariff Act which contains elaborate classification of goods and rate structure of duties. However, these rates are liable to be changed from time to time. Further, while the levy is on the manufacture or production of goods, the stage of collection need not, at a point of time, synchronise with the completion of the manufacturing.

These principles are in fact, embodied in the Central Excise Law in as much as Section 3 of the Act stipulates 'manufacture' as the taxable event, Rule 4 of the Central Excise Rules, on the other hand, stipulates 'removal of goods from the factory' or any other specified places as the point of time for collection of duty.

2. DUTY PAYABLE ON REMOVAL (RULE 4)

- Every person who produces or manufactures any excisable goods, or who stores such goods in a warehouse, shall pay the duty leviable on such goods in the manner provided in rule 8 or under any other law, and
- No excisable goods, on which any duty is payable, shall be removed without payment of duty from any place, where they are produced or manufactured, or from a warehouse, unless otherwise provided.
- Where molasses are produced in a khandsari sugar factory, the person who procures such molasses, whether directly from such factory or otherwise, for use in the manufacture of any commodity, whether or not excisable, shall pay the duty leviable on such molasses, in the same manner as if such molasses have been produced by the procurer.

- Raw material supplier is liable to pay duty with respect to readymade garments and made ups under chapters 61, 62 and 63 of CETA.
- Commissioner may, in exceptional circumstances having regard to the nature of the goods and shortage of storage space at the premises of the manufacturer where the goods are made, permit a manufacturer to store his goods in any other place outside such premises, without payment of duty subject to such conditions as he may specify.

3. REMOVAL OF GOODS ON INVOICE (RULE 11)

It has been provided under Rule 4 of the Central Excise Rules, 2002 that excisable goods can be removed from the place of their manufacture/production only on payment of duty, unless otherwise provided. Rule 8 lays down the provisions allowing payment of duty on monthly basis thereby allowing clearance of goods from the factory without payment of duty.

The provisions relating to removal of goods on an invoice are contained under Rule 11 of these Rules. Sub-rule (1) of Rule 11 provides that

- no excisable goods shall be removed from a factory or a warehouse except under an invoice signed by the owner of the factory or his authorised agent and
- in case of cigarettes each such invoice is required to be countersigned by the Inspector of Central Excise or the Superintendent of Central Excise before the Cigarettes are removed from the factory.

Invoice should be serially numbered and contain

- the registration number,
- description,
- classification,
- time and date of
- removal, rate of duty,
- quantity and value of goods alongwith duty payable,
- mode of transport and registration number of vehicle thereon [Sub-rule (2)].
- Address of the divisional office of A.C / D.C

Rule 11(3) provides that invoice shall be prepared in triplicate and is required to be marked as under:

- (i) Original copy being marked as ORIGINAL FOR BUYER;
- (ii) Duplicate copy being marked as DUPLICATE FOR TRANSPORTER;
- (iii) Triplicate copy being marked as TRIPPLICATE FOR ASSESSEE.

At a time, only one copy of invoice book shall be in use unless otherwise allowed by Assistant/Deputy Commissioner, as the case may be, in the special facts and circumstances of each case [Sub-rule (4)].

Before making use of the invoice book, the serial numbers of the same shall be intimated to the Superintendent of Central Excise having jurisdiction.

The provisions of this rule shall apply mutatis mutandis to goods supplied by a first stage dealer or a second stage dealer.

4. DATE FOR DETERMINATION OF DUTY AND TARIFF VALUATION (RULE 5)

- The rate of duty or tariff value applicable to any excisable goods, other than khandsari molasses, shall be the rate or value in force on the date when such goods are removed from a factory or a warehouse, as the case may be.
- The rate of duty in the case of khandsari molasses, shall be the rate in force on the date of receipt of such molasses in the factory of the procurer of such molasses.

Explanation - If any excisable goods are used within the factory, 'the date of removal of such goods' shall mean the date on which the goods are issued for such use.

The question therefore arises as to what rate of duty will be charged, if goods manufactured on one date are removed on a later date and in the meantime, the rate of duty applicable to the goods in question undergoes an upward revision or if the goods in question were not liable to duty when they were manufactured but on the date of removal they became liable to duty? In such a situation, while Rule 5(1) of the Central Excise Rules provides that the rate of duty and tariff valuation applicable to any excisable goods other than khandsari molasses shall be the rate and value in force on the date of removal of goods from the factory or warehouse, as the case may be, the contention of the manufacturer, invariably would be that the manufacture being the taxable event, the rates prevailing on the date of manufacture should be levied.

The rate of duty in the case of Khandsari molasses, shall be the rate in force on the date of receipt of such molasses in the factory of the procurer of such molasses. It has also been provided in the Explanation to Rule 5(2) that if any excisable goods are used within the factory, the date of removal of such goods shall mean the date on which the goods are issued for such use.

As per Sub-rule (3) of this Rule, rate of duty in the case of goods falling under Chapter 62 of the First Schedule to the Central Excise Tariff Act 1985, produced or manufactured on job work, shall be the rate in force on the date of removal of such goods by the person getting the goods manufactured under the aforestated Chapter.

5. MANNER OF PAYMENT OF DUTY (RULE 8)

Rule 8 of the Central Excise Rules, 2002 lays the provisions relating to manner of payment of duty. Goods are cleared from the factory under an invoice and the duty is paid either by cash and/or CENVAT Credit.

(a) In case of Non-SSI (Small Scale Industry)

As per sub rule 1 of this rule, the duty on the goods removed from the factory or the warehouse during a month shall be paid by

- the 6th day of the following month, if the duty is paid electronically through internet banking and
- by the 5th day of the following month, in any other case.

The duty shall be paid by the 31st day of March where the goods are removed during the month of March.

(b) In case of SSI

Where an assessee is availing of the exemption under a notification based on the value of clearances in a financial year, the duty on goods cleared during a calendar month shall be paid by –

- the 6th day of the following quarter if the duty is paid electronically through internet banking and
- the 5th day of the following quarter, in any other case,

The duty shall be paid by the 31st day of March where the *goods are removed during the quarter ending March.*

(c) E-payment of duty

It is mandatory to pay the duty electronically where an assessee has paid duty of one lakh rupees or more, including the amount of duty paid by utilization of CENVAT credit, in the preceding financial year.

(d) Consequences where the assessee fails to pay the duty by due date

If the assessee fails to pay the amount of duty by due date, he shall be liable to pay the outstanding amount along with interest at the rate specified by the Central Government vide notification under section 11AA of the Act on the outstanding amount, for the period starting with the first day after due date till the date of actual payment of the outstanding amount.

If the assessee defaults in payment of duty beyond thirty days from the due date, as prescribed in sub-rule (1), then notwithstanding anything contained in said sub-rule (1) and sub-rule (4) of rule 3 of CENVAT Credit Rules, 2004, the assessee shall, pay excise duty for each consignment at the time of removal, without utilizing the CENVAT credit till the date the assessee pays the outstanding amount including interest thereon; and in the event of any failure, it shall be deemed that such goods have been cleared without payment of duty and the consequences and penalties as provided in these rules shall follow.

The provisions of section 11 of the Act shall be applicable for recovery of the duty as assessed under rule 6 and the interest under sub-rule (3) in the same manner as they are applicable for recovery of any duty or other sums payable to the Central Government.

Explanation: For the purposes of this rule, the expressions 'duty' or 'duty of excise' shall also include the amount payable in terms of the CENVAT Credit Rules, 2004.

STORAGE OF GOODS: MAINTENANCE OF DAILY STOCK ACCOUNT (RULE 10)

The assessee is required to maintain proper accounts (though no statutory records are required) to prove the authenticity of quantities of manufacture and removal etc. Rule 10 provides for the maintenance of *DAILY STOCK ACCOUNT* which must be maintained by the assessee. The following points are relevant under this:

- The DSA is to be maintained on daily basis. Entries be made immediately when goods manufactured are stored in a store room.
- Any removal from the factory must be duly recorded in DSA
- The DSA to contain the details regarding
 - (a) description of goods manufactured,
 - (b) opening stock,
 - (c) quantity produced,
 - (d) inventory of goods,
 - (e) quantity removed,
 - (f) assessable value,
 - (g) amount of duty payable and paid.

The first page and the last page of each account book must be duly authenticated by the manufacturer/ the authorised agent.

All such records must be preserved for a period of 5 years.

- Any violation such as non maintenance of records/ non entry/ wrong entry in records may entail penalty upto 100% of duty and confiscation may also be possible.[rule 25(1)(b)]
- Duty liability arises as soon as the goods are stored in the store room in fully manufactured condition.
- There may be remission of duty when the goods are lost, destroyed evaporated etc due to natural causes or circumstances beyond the control of the assessee.
- Such loss may be during storage/ transit between places of removal.

JOB WORK IN ARTICLE OF JEWELLERY (RULE 12AA)

Every person (not being an export-oriented unit or a unit located in special economic zone) who gets article of jewellery produced or manufactured on his behalf, on job work basis, shall obtain registration, maintain accounts, pay duty leviable on such goods and comply with all the relevant provisions of these rules, as if he is an assessee [Rule 12AA (1)].

As per rule 12AA(2), if the said person desires clearance of excisable goods for home consumption or for exports from the premises of the job worker, he shall pay duty on such excisable goods and prepare an invoice, in the manner referred to in rules 8 and 11 respectively except for mentioning the date and time of removal of goods on such invoice.

The original and the duplicate copy of the invoice so prepared shall be sent by him to the job worker before the goods are cleared from the premises of the job worker. The job worker shall fill up the particulars of date and time of removal of goods before the clearance of goods and after such clearance the job worker shall intimate to the said person, the date and time of the clearance of goods for completion of the particulars by the said person in the triplicate copy of the invoice.

The said person may supply or cause to supply to a job worker, the following goods, namely:-

- (a) inputs in respect of which he may or may not have availed CENVAT credit in terms of the CENVAT Credit Rules, 2004, without reversal of the credit thereon; or
- (b) goods manufactured in the factory of the said person without payment of duty; under a challan, consignment note or any other document with such information as specified in sub-rule (2) of rule 11 of the Central Excise Rules, 2002, duly signed by him or his authorised agent.

The job worker shall not be required to get himself registered or shall not be required to maintain any record evidencing the processes undertaken for the sole purposes of undertaking job work.

The job worker, with or without completing the job work may,-

- (i) return the goods without payment of duty to the said person; or
- (ii) clear the goods for home consumption or for exports subject to receipt of an invoice from the said person.

As per Rule 12AA(9), the job worker shall clear the goods after filling in invoice the time and date of removal and authentication of such details. The rate of duty on such goods shall be the rate in force on date of removal of such goods from the premises of the job worker and no excisable goods shall be removed except under the invoice.

Job worker means a person engaged in manufacture or processing on behalf and under the instructions of the said person from any inputs or goods supplied by the said person or by any other person authorized by

the said person, so as to complete a part or whole of the process resulting ultimately in manufacture of articles of jewellery falling under heading 7113 of the First Schedule to the Central Excise Tariff Act, 1985, and the term "job work" shall be construed accordingly.

Brand name or trade name means a brand name or trade name, whether registered or not, that is to say, a name or a mark, such as a symbol, monogram, label, signature or invented words or any writing which is used in relation to a product, for the purpose of indicating, or so as to indicate, a connection in the course of trade between the product and some person using such name or mark with or without any indication of the identity of that person.

If any goods or part thereof is lost, destroyed, found short at any time before the clearance of articles of jewellery or waste, by-products or like goods arising during the course of manufacture of such goods, the said person shall be liable to pay duty thereon as if such goods were cleared for home consumption.

PROCEDURE AND FACILITIES FOR LARGE TAXPAYER (RULE 12BB)

A large taxpayer may remove excisable goods, except

- motor spirit, commonly known as petrol, high speed diesel and light diesel oil (hereinafter referred to as the intermediate goods),
- without payment of duties of excise, under the cover of a transfer challan or invoice, from any of his registered premises, (hereinafter referred to as the sender premises)
- where such goods are produced, manufactured or warehoused to his other registered premises, other than a premises of a first or second stage dealer (herein after referred to as the recipient premises),
- for further use in the manufacture or production of such other excisable goods (hereinafter referred to as the subject goods) in recipient premises subject to condition that
 - the subject goods are manufactured or produced using the said intermediate goods and
 - cleared on payment of appropriate duties of excise leviable thereon within a period of six months,
 - from the date of receipt of the intermediate goods in the recipient premises; or
 - the subject goods are manufactured or produced using the said intermediate goods and exported out of India, under bond or letter of undertaking within a period of six months, from the date of receipt of the intermediate goods in the recipient premises, and
- that any other conditions prescribed by the Commissioner of Central Excise, Large Taxpayer Unit in this regard are satisfied.

If the subject goods manufactured or produced using the said intermediate goods are not cleared on payment of appropriate duties of excise leviable thereon or are not exported out of India within the said period of six months, duties of excise payable on such intermediate goods shall be paid by the recipient premises with interest in the manner and rate specified under section 11AA of the Act.

Illustration

Excise duty is payable on intermediate goods, namely, electronics goods, manufactured by factory A which are removed without payment of duties of excise for use in the manufacture of subject goods, namely, machines, in factory B of the large taxpayer. In case such machines are not exported or are removed without

payment of duties of excise, then factory B shall pay duties of excise payable on the electronic goods so cleared along with interest.

If any duty of excise is payable on such intermediate goods and if the said duty is not payable on such subject goods, the said duty of excise as equivalent to the total amount payable on such intermediate goods along with interest under section 11 AB of the Act shall be paid by the recipient premises.

Illustration

National Calamity Contingent duty is payable on intermediate goods namely, polyester yarn manufactured by factory A. Such yarn is removed without payment of duty of excise for use in the manufacture of subject goods, namely, grey fabrics in factory B of a large taxpayer, (on which such National Calamity Contingent duty is not payable), then factory B shall pay an amount equivalent to the National Calamity Contingent duty that would have been payable on the polyester yarn along with interest under section 11AB of the Act.

The transfer challan or invoice shall be serially numbered and shall contain the registration number, name, address of the large taxpayer, description, classification, time and date of removal, mode of transport and vehicle registration number, quantity of the goods and registration number and name of the consignee:

The duty payable under the first and second proviso shall be the duty payable on the date and time of removal of the intermediate goods from the sender s premises.

The facility of large tax payer unit shall not be available;

- if the recipient premises is availing Exemption notifications.
- to a export oriented unit or a unit located in a Electronic Hardware Technology Park or Software Technology Park.

If a large taxpayer fails to pay any amount due in terms of the first and second provisos, it shall be recovered along with interest in the same manner as provided under section 11A and section 11AA respectively of the Act.

Where a registered premises of a large taxpayer manufacturing excisable goods has paid to the credit of Central Government any duty of excise in excess of duty of excise payable on account of arithmetical error, the said large taxpayer may adjust the excess duty so paid by him, against his duty liability for the subsequent period subject to the limitations prescribed under clause (b) of sub-rule (7) of rule 3 of the CENVAT Credit Rules, 2004.

However, such adjustment shall be admissible only if the said registered premise has not passed on the incidence of such excess duty so paid to any other person, and the consignee does not avail credit of such duty under the said CENVAT Credit Rules, 2004.

Any notice issued but not adjudged by any of the Central Excise officer administering the Act or rules made thereunder immediately before the date of grant of acceptance by the Chief Commissioner of Central Excise, Large Taxpayer Unit, shall be deemed to have been issued by Central Excise officers of the said Unit.

A large taxpayer shall submit the monthly returns, as prescribed under these rules, for each of the registered premises.

A large taxpayer, on demand, may be required to make available the financial, production, stores and CENVAT credit records in electronic media, such as, compact disc or tape for the purposes of carrying out any scrutiny and verification as may be necessary.

A large taxpayer may, with intimation of at least thirty days in advance, opt out to be a large taxpayer from the first day of the following financial year.

MAINTENANCE OF RECORDS AND PAYMENT OF DUTY BY THE INDEPENDENT WEAVER OF UNPROCESSED FABRICS (RULE 12C)

An independent weaver of unprocessed fabrics falling under Chapter 50, 51, 52, 53, 54, 55, 58 or 60 of the First Schedule to the Tariff Act, may, at his option, authorize another person, on his behalf, to maintain accounts, pay duty, prepare invoice and comply with any of the provisions of these rules except that of rule 9:

However, primary responsibility to comply with the provisions of these rules shall lie with the said independent weaver and in case of short payment or non-payment of duty on such unprocessed fabrics; consequences and penalties shall apply both to the said independent weaver and his authorized agent.

Independent weaver means a weaver who works on his own, purchases the yarn himself and sells the grey fabrics manufactured by him.

POWER TO IMPOSE RESTRICTIONS IN CERTAIN TYPES OF CASES (RULE 12CCC)

where the Central Government, having regard to the extent of evasion of duty, nature and type of offences or such other factors as may be relevant, is of the opinion that in order to prevent evasion of, or default in payment of duty of excise, it is necessary in the public interest to provide for certain measures including restrictions on a manufacturer, first stage and second stage dealer or an exporter may, by notification in the Official Gazette, specify the nature of restrictions including suspension of registration in case of a dealer, types of facilities to be withdrawn and procedure for issue of such order by the Chief Commissioner of Central Excise.

Explanation.- For the purposes of this rule, it is hereby clarified that every proposal initiated in terms of the procedure specified under notification no. 05/2012-CE (N.T.) dated the 12th March, 2012 published in the Gazette of India, Part II, Section 3, Sub-section (i) vide number G.S.R. 140(E), dated the 12th March, 2012, which is pending, shall be treated as initiated in terms of the procedure specified under this rule and shall be decided accordingly.

COMPOUNDED LEVY SCHEME (RULE 15): SPECIAL PROCEDURE FOR PAYMENT OF DUTY

Compounding of levies implies the assessee being authorised to pay a pre-determined sum to the department, at fixed periodical intervals, instead of paying duty on a consignment-to-consignment basis. The amount of duty to be paid is pre-determined by the department on the basis of various parameters pertaining to production.

The advantage of compounding is that the assessee is freed from the procedural formalities being fulfilled by him for each consignment. The advantage to the department is that it reduces the need to control various factors pertaining to production and removal. The option has been made available in case of manufacturers in unorganised sectors where accounting records are not adequate or proper for consumption and collection of duty payable on goods manufactured.

The Central Government may, by notification, specify the goods in respect of which an assessee shall have the option to pay the duty of excise on the basis of such factors as may be relevant to production of such goods and at such rate as may be specified in the said notification, subject to such limitations and conditions, including those relating to interest or penalty, as may be specified in such notification.

The Central Government may also specify by notification the manner of making an application for availing of

the special procedure for payment of duty, the abatement, if any, that may be allowed on account of closure of a factory during any period, and any other matter incidental thereto.

It may be noted that compounded levy scheme (CLS) is similar to payment under production capacity scheme under Section 3A.

But there are differences. Cess is payable on amount paid under compounded levy scheme whereas it is not payable under Section 3A.

Compounded Levy Scheme is an optional scheme but Section 3A is a mandatory scheme. Even products notified under both the schemes are different.

CREDIT OF DUTY ON GOODS BROUGHT TO THE FACTORY (RULE 16)

Where any goods on which duty had been paid at the time of removal thereof are brought to any factory for being re-made, refined, re-conditioned or for any other reason, the assessee shall state the particulars of such receipt in his records and shall be entitled to take CENVAT credit of the duty paid as if such goods are received as inputs under the CENVAT Credit Rules, 2002 and utilise this credit according to the said rules.

If the process to which the goods are subjected before being removed does not amount to manufacture, the manufacturer shall pay an amount equal to the CENVAT credit taken and in any other case the manufacturer shall pay duty on goods received at the rate applicable on the date of removal and on the value determined under subsection (2) of section 3 or section 4 or section 4A of the Act, as the case may be.

The amount paid shall be allowed as CENVAT credit as if it was a duty paid by the manufacturer who removes the goods.

If there is any difficulty in following the provisions of sub-rule (1) and sub-rule (2), the assessee may receive the goods for being re-made, refined, re-conditioned or for any other reason and may remove the goods subsequently subject to such conditions as may be specified by the Commissioner.

Assessee shall include wire drawing unit, which has cleared the goods on payment of an amount equal to the duty at the rate applicable to drawn wire on the date of removal and on the value determined under relevant provisions of the Act and the rules made thereunder.

The amount paid under the first proviso shall be allowed as CENVAT credit as if it was duty paid by the assessee who removes the goods.

REMOVAL OF GOODS FOR JOB WORK, ETC. (RULE 16A)

Any inputs received in a factory may be removed as such or after being partially processed to a job worker for further processing, testing, repair, re-conditioning or any other purpose subject to the fulfillment of condition specified in this behalf by the Commissioner of Central Excise having jurisdiction.

SPECIAL PROCEDURE FOR REMOVAL OF SEMI-FINISHED GOODS FOR CERTAIN PURPOSES (RULE 16B)

The Commissioner of Central Excise may by special order and subject to conditions as may be specified by the Commissioner of Central Excise, permit a manufacturer to remove excisable goods which are in the nature of semi-finished goods, for carrying out certain manufacturing processes, to some other premises and to bring back such goods to his factory, without payment of duty, or to some other registered premises and allow these goods to be removed on payment of duty or without payment of duty for export from such other registered premises.

SPECIAL PROCEDURE FOR REMOVAL OF EXCISABLE GOODS FOR CARRYING OUT CERTAIN PROCESSES (RULE 16C)

The Commissioner of Central Excise may, by special order and subject to such conditions as may be specified by him, permit a manufacturer to remove excisable goods manufactured in his factory, without payment of duty, for carrying out tests or any other process not amounting to manufacture, to any other premises, whether or not registered, and after carrying out such tests or any such other process may allow,-

- (a) bringing back such goods to the said factory without payment of duty, for subsequent clearance for home consumption or export, as the case may be, or
- (b) removal of such goods from the said other premises, for home consumption on payment of duty leviable thereon or without payment of duty for export, as the case may be.

This rule shall not apply to the goods known as "prototypes" which are sent out for trial or development test.

REMISSION OF DUTY (RULE 21)

Section 5 of the Central Excise Act, 1944, empowers the Central Government to make rules providing for remission of duty on loss of quantity due to natural causes.

Remission means cancellation or waiver of duty.

The manufacturer has to make an application to the appropriate authority for remission of duty for the loss of goods in the store room. The remission may be granted by various authorities depending upon the amount involved. The remission of duty may be claimed by the manufacturer at any time before removal.

Grounds for remission of duty

- Natural causes
- Unavoidable accident or
- Unfit for consumption or marketing

Amount which may be granted by the authorities:

Amount of Remission (₹)	Appropriate Authority
Upto 10,000	Superintendent of Central Excise
Above 10,000 upto 1,00,000	Assistant /Deputy Commissioner of Central Excise
Above 1,00,000 upto 5,00,000	Joint/Additional Commissioner of Central Excise
Above 5,00,000	Commissioner of Central Excise

FILING OF RETURN (RULE 12)

Rule 12 of the Central Excise Rules, 2002 lays down the provisions relating to filing of return. As per Sub-rule (1) of this Rule,

- every assessee is required to submit a monthly return in proper form of production or removal of goods and
- other relevant particulars to the superintendent of Central Excise,

within ten days after the close of the month to which the return relates.

It has also been provided that where an assessee is availing the exemption under a notification based on the

value of clearances in a financial year, he shall file a quarterly return in proper form of production and removal of goods and other relevant particulars within 10 days after the close of the quarter to which the return relates. According to Notification, the return is required to be filed in quintuplicate in Form ER-1 (EOU/EPZ/SEZ units are required to file return in Form ER-2). For SSIs, Form ER-3 has been prescribed.

If there is delay in payment of duty, interest should also be deposited before filing ER-1 return. This return is acknowledged by Superintendent of Central Excise and one copy duly acknowledged is returned to the assessee.

Annual Financial Information Statement

Every assessee shall submit to the Superintendent of Central Excise, an Annual Financial Information Statement for the preceding financial year to which the statement relates in Form E.R. 4 - **by 30th day of November of the succeeding year.**

The Central Government may, by notification, and subject to such conditions or limitations as may be specified in such notification, specify assessee or class of assessees who may not require to submit such an Annual Financial Information Statement.

Annual Information Installed Capacity Statement

Every assessee shall submit to the Superintendent of Central Excise, an Annual Installed Capacity Statement declaring the annual production capacity of the factory for the financial year to which the statement relates in the form E.R 7- **by 30th day of April of the succeeding financial year.**

The Central Government may, by notification, and subject to such conditions or limitations as may be specified in such notification, specify assessee or class of assessees who may not require to submit such an Annual Installed Capacity Statement.

The proper officer may on the basis of information contained in the return filed by the assessee under sub-rule (1), and after such further enquiry as he may consider necessary, scrutinize the correctness of the duty assessed by the assessee on the goods removed, in the manner to be prescribed by the Board.

As per Rule 12(3), the proper officer has power to scrutinize the correctness of the duty assessed by assessee based on the return filed or further enquiry.

Rule 12(4): The assessee has to make available all the documents and records for verification by proper officer.

VARIOUS RETURNS SUBMITTED UNDER RULES			
RETURN	ASSESSSEE	PERIODICITY/ TYPE	TIME LIMIT
ER-1 [Rule 12(1) of CE Rules, 2002]	Non SSI units	Monthly Return to superintendent	By 10 th of the following month.
ER-2 [Rule 12(1) of CE Rules, 2002]	EOUs	Monthly Return to superintendent	By 10 th of the following month
ER-3 [Rule 12(1) of CE Rules, 2002]	SSI units availing exemption	Quarterly, Return to superintendent	By 10 th of the following quarter
Form A [Rule 12(1)]	Units availing area based	Quarterly, Return to Assistant	By 20 th of the following

of CE Rules, 2002]	exemption.	Commissioner	quarter
ER-4 [Rule 12(2) of CE Rules, 2002]	Assesseees paying ₹ one crore or above (through cash + cenvat credit).	Annual, Annual Financial Information Statement electronically.	Annual. By 30 th of November of following year.
ER-7 [Rule 12(2A) of CE Rules, 2002]	Every assessee is required to file Annual installed capacity statement	Annual return declaring the annual production capacity of previous year	Annually by 30 th April
ER-8 [Rule 12 Proviso]	Assesseees availing exemption under notification No. 1/ 2011 have to file quarterly return of production and removal of goods etc.	Quarterly return	Within 10 days.

ELECTRONIC FILING (E-FILING OF RETURN)

E-filing of returns is mandatory now for all assesseees irrespective of amount of duty paid. Earlier, only assesseees making e-payment mandatorily were required to submit returns electronically and for all others it was optional.

But now, all assesseees, including those whose tax liability is nil, are required to submit returns electronically.

Even EOUs under Rule 17 are required to make e-filing.

Even specified assesseees under Rule 9A of Cenvat Credit Rules have to submit returns/ statements on principal inputs electronically.

Exception: Assesseees enjoying area based exemption under notification No. 49/ 2003 & 50/ 2003 are not required to make e-filing.

RULE 17 REMOVAL OF GOODS BY E.O.U FOR D.T.A

In case of removal of goods in the Domestic Tariff Area(DTA) by EOUs. the same procedure is to be followed with regard to accounting, clearance etc.

(1) The EOU has to remove goods under invoice. The appropriate duty [import duty as per Proviso to Section 3 (1)] has to be paid by utilizing the CENVAT credit or by crediting the duty payable to the account of the Central Government in the manner specified in rule 8.

(2) Proper accounts regarding goods, description duty paid etc. as prescribed by BOARD have to be maintained.

(3) Appropriate monthly return in the prescribed form [E.R 2] has to be submitted by 10th of the following month relating to inputs, capital goods and goods manufactured.

(4) The proper officer may on the basis of information contained in the return filed by the unit under sub-rule (3), and after such further enquiry as he may consider necessary, scrutinise the correctness of the duty assessed by the assessee on the goods removed, in the manner to be prescribed by the Board.

(5) Every assessee shall make available to the proper officer all the documents and records for verification as and when required by such officer.

WAREHOUSING PROVISIONS (RULE 20)

(1) The Central Government may by notification, extend the facility of removal of any excisable goods from the factory of production to a warehouse, or from one warehouse to another warehouse without payment of duty.

(2) The facility shall be available subject to such conditions, including penalty and interest, limitations, including limitation with respect to the period for which the goods may remain in the warehouse, and safeguards and procedure, including in the matters relating to dispatch, movement, receipt, accountal and disposal of such goods, as may be specified by the Board.

(3) The responsibility for payment of duty on the goods that are removed from the factory of production to a warehouse or from one warehouse to another warehouse shall be upon the consignee.

(4) If the goods dispatched for warehousing or re-warehousing are not received in the warehouse, the responsibility for payment of duty shall be upon the consignor.

POWER TO ISSUE SUPPLEMENTARY INSTRUCTIONS (RULE 31)

The Board or the Chief Commissioner or the Commissioner, may issue written instructions providing for any incidental or supplemental matters, consistent with the provisions of the Act and these rules.

TRANSITIONAL PROVISION (RULE 33)

Any notification, circular, instruction, standing order, trade notice or other order issued under the Central Excise (No. 2) Rules, 2001 by the Board, the Chief Commissioner or the Commissioner of Central Excise, and in force as on the 28th day of February, 2002, shall, to the extent it is relevant and consistent with these rules, be deemed to be valid and issued under the corresponding provisions of these rules.

EXCISE DUTY — EXEMPTIONS

To recapitulate, democracy, as even the word etymologically indicates, is the power of the people. The rulers rule, because the people have authorised them to rule. While every power exercised by a democratic government must have the sanction of the people, the important power of taxation is also subject to the same principle that it should be authorised by the people. This concept is enshrined in Article 265 of our Constitution which states “no tax shall be levied or collected except by authority of law”.

In pursuance of the principle and constitutional prescription as examined above, Union Excise Duties are levied by virtue of the power conferred upon the Government by the Union Legislature through the Central Excise Act, 1944 (hereinafter referred to as the ‘Act’). Section 3 of the Act explicitly states that duties of excise on goods produced or manufactured in India shall be levied at the rates specified in the First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985.

The rates prescribed in the Central Excise Tariff are termed as ‘statutory rates’ since these are the rates prescribed in the statute. Often times, they are also referred to as ‘standard rates’ or ‘tariff rates’.

Problems faced in administration of indirect taxes

While the legislature alone has the power to prescribe rates of taxation, indirect taxes like Excise and Customs, however, pose a problem which makes it almost impossible to observe this principle to the hilt. The tax base for indirect taxes is the entire field of manufacturing industry and trade. Once this is noted, the fact which immediately should strike one is that it is not a static field, but a field which exhibits ebullient dynamism. In this field, most factors change frequently and fast. New products, new processes, new marketing methods etc. are constantly thrown up. To suit the ever changing needs and match the features of a dynamic tax base like industry and trade, the fiscal administration should also be equipped with the ability to vary the rates whenever emergent situations warrant such variations.

Thus, while flexibility should be a very important feature of tax rates in commodity taxation, the basic principle of legislative mandate for each change of rate of duty would militate considerably against it.

While the legislature can no doubt change the rates of duty prescribed by it (statutory rates), still it is common knowledge that the legislative process itself is quite elaborate and time consuming. Hence, while on the one hand, rates of duty have to be altered with utmost despatch, on the other, it may not be possible to have it done through the legislative process. The solution to the problem is through the instrument of duty exemptions.

The concept of exemptions

Flexibility in the matter of rates of duty of excise is brought through the power vested in the executive arm of the Government by the legislature itself, to reduce the rates of duty from what the statutory rates is. Section 5A of the Central Excise Act, 1944, confers this power on the Government.

POWER TO GRANT EXEMPTION FROM DUTY OF EXCISE (SECTION 5A)

Section 5A(1) of the Central Excise Act, 1944 empowers the Central Government to exempt any excisable goods either from the whole of duty prescribed (the statutory rate) or a part thereof. Each such an exemption should be announced through a Notification in the Gazette of India.

- The exemption may be a 'straight exemption', that is, without any condition attached to it, or it may be a 'conditional exemption' to which only assessee fulfilling the conditions specified are eligible.
- Sub-section (1A) lays that where an exemption under Sub-section (1) in respect of any excisable goods from the whole of the duty of excise leviable thereon has been granted absolutely, the manufacturer of such excisable goods shall not pay the duty of excise on such goods.
- Sub-section (2) empowers the Central Government to grant exemption from duty of excise by special order in each case under circumstances of an exceptional nature to be stated in such order.
- The Government however does not change any power under Section 5A(2) to exempt goods partly from duty, unlike the cases of General Exemptions under Section 5A(1). Further, whereas the exemptions given by the Central government under Section 5A(1) will be communicated through a notification published in the Official Gazette, the exemptions given under Section 5A(2) will be communicated through *special orders*.
- Sub-section (2A) to Section 5A empowers the Central Government to insert an explanation to such notification or order issued under Sub-sections (1) or (2) for the purpose of clarifying the scope or applicability of the notification / order as the case may be, by way of notification in the official Gazette at any time within one year of the issue of above notification/ order.

- Every such explanation shall have effect as if it had always been the part of the notification issued or order passed under Sub-sections (1) and (2) of Section 5A of the Act, which means, it has retrospective effect.

While the Government is thus empowered to give duty relief through exemptions, the question arises whether utilising this instrument, the Government can change the rate structure itself. They can do so, since Section 5A(3) states that through exemptions, rates of duty may be prescribed in 'a form or method' different from what obtains in the statutory rate. Thus, while the statutory rate may be on the basis of value (ad valorem rate), through an exemption, it may be converted into a rate based on quantity (specific rate) or vice versa. The important condition is that by such conversion through exemptions, the quantum of duty should not exceed what is authorised by the statutory rate. The parliamentary control over taxation is supreme and inviolable.

Sub-section (4) of Section 5A provides that every notification issued under Sub-rule (1) and in force immediately before the commencement of the Customs and Central Excise Laws Amendment Act, 1988 shall be deemed to have been issued or made under the provisions of this section and shall continue to have the same force and effect after such commencement until amended, varied, rescinded or superseded under the provisions of Section 5 of the Central Excise Act, 1944.

As per Sub-section (5) of Section 5A, "every notification issued under Sub-section (1) or Sub-section (2) shall:

- unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette;
- also be published and offered for sale on the date of its issue by the Directorate of Publicity and Public Relations, Customs and Central Excise, New Delhi, under the Central Board of Excise and Customs constituted under the Central Board of Revenue Act, 1963 (54 of 1963).

As per Sub-section (6), notwithstanding anything contained in Sub-section (5), where a notification comes into force on a date later than the date of its issue, the same shall be published and offered for sale by the said Directorate of Publicity and Public Relations on a date on or before the date on which the said notification comes into force.

In order to put the matter beyond all doubt and minimise disputes it is statutorily provided that unless it is specified otherwise, an exemption notification shall come into effect on the date of its issue. As stated earlier this is to remove the practical problem resulted by the Supreme Court judgement in *Collectors v. New Tobacco Co. - 1998 (97) E.L.T. 388 (S.C.)*.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What is the need for exercising continuous control by the department over manufacturers of excisable goods?
2. What do you mean by assessment of duty under Central Excise? What does it include explain.
3. Explain the provisions relating to storage and treatment of storage losses?
4. What are the consequences of non payment of duty?
5. What is the procedure to be followed by EOUs ?

6. What is compounded levy scheme? How is it different from production capacity scheme under Section 3A?
7. What are the objectives of providing for “exemptions”?
8. What are the different types of exemptions which could be given under the provisions of laws on Central Excise?
9. How these exemptions can be availed within the provisions of law on excise?
10. From which date does an exemption Notification becomes effective? State with the help of example and case law.
11. Does the law on excise empower the issue of notifications for exemptions only or can it also be used for increase in rate of duty? If yes, State the circumstances and limitations, if there is any.

SUGGESTED READINGS

- (1) Excise Manual, *Cbec.gov.in*
- (2) Central Excise Manual — *R.K. Jain*
- (3) Excise Law Times — *Centax Publications Pvt. Ltd.*

CENTRAL EXCISE LAW

PART V: CENVAT CREDIT RULES, 2004

After completion of this part the students will have the understanding of;

- What constitute input, input services, exempted goods, exempted services, capital goods etc.
- Eligible taxes and duties for which credit can be taken
- What are conditions to be fulfilled for taking and utilizing credit
- Procedure for availing Cenvat credit
- Documents/records to be maintained

INTRODUCTION

In India, prior to introduction of CENVAT the concept of MODVAT (Modified Value Added Tax) was there. MODVAT (Modified Value Added Tax) was introduced in India in 1986 (re-named as CENVAT w.e.f 1.4.2000). The system was termed as MODVAT, as it was restricted up to the manufacturing stage and credit of only excise duty paid on manufacturing products (and corresponding CVD paid on imported goods) was available.

MODVAT - ORIGIN OF THE CONCEPT

Introduced as a part of the Budget speech in 1986 and brought into being through the Central Excise (Seventh Amendment) Rules, 1986 with effect from 1.3.1986 vide Central Excise Notification No. 176 of 1986, the scheme came to be known as Modified Value Added Tax, in short MODVAT.

The Scheme was an outcome of a detailed and indepth analysis of the entire problem of cascading effect of duties inherent in indirect taxes, by the Indirect Taxation Enquiry Committee of 1976 under the Chairmanship of the renowned economist Late Shri L.K. Jha. The Committee suggested that the Government may take a few experimental steps, to start with, and introduce a modified version of VAT (i.e. Value Added Tax) prevalent in most of the European Countries and named it as "MANVAT", as it was to be confined to the manufacturing stage alone and not to sales tax also as is normally the case in a pure VAT system.

Based on the studies and considering the long overdue need, in the Budget Speech for 1985-86, the then Finance Minister made a commitment to move towards a Long-term Fiscal Policy co-terminous with the plan. In response to that commitment, the Long Term Fiscal Policy was announced in December, 1985 and this Policy contained for the first time the proposal to introduce MODVAT. This proposal took concrete shape when the Finance Minister moved the Budget for 1986-87, announcing therein the introduction of MODVAT Credit Scheme with effect from 1st March, 1986.

The MODVAT Scheme which was initially confined to only specified excisable goods used as inputs and was contained in Rules 57A to 57JJ of the Central Excise Rules, 1944 was further extended to cover capital goods in its scope and a separate Section 'AAAA' was inserted in Chapter V of the Central Excise Rules, detailing the scheme under Rules 57Q to 57U. These rules were then notified vide Notification No. 6/97 CE (N.T) dated 1.3.97 which lost its effect vide Notification No. 27/2000-CE(NT) dated 31.3.2000.

CENVAT — INTRODUCTION

CENVAT Scheme conforming to introduction of CENVAT (Central Value Added Tax) has come into

existence pursuant to the statement made by the Hon'ble Finance Minister in his Budget Speech for the year 2000-2001. This scheme provided a small set of simple and transparent rules in order to put an end to the disputes arising between the Department and the assessees relating to interpretation of MODVAT rules and procedures.

As a measure of rationalisation, Budget 2000 established a single rate of 16% Central Value Added Tax (CENVAT) at the Centre by converging existing three ad valorem rates of 8%, 16% and 24% prescribed by Budget 1999. Pursuant to this, the MODVAT scheme in force till 31.3.2000 is rechristened as CENVAT Scheme and the Central Excise Rules pertaining to credit on inputs and capital goods were revised under a new series of Rules 57A to 57V vide Budget Notification 11/2000-CE(NT) dated 1.3.2000 for the then existing Rules 57A to 57JJ and 57Q to 57U. However, these rules were again re-written and got substituted by new series of Rules 57AA to 57AK vide Notification 27/2000-CE(NT) dated 31.3.2000 effective from 1.4.2000, even before the implementation of earlier series of Rules 57A to 57V.

With effect from 1.7.2001 Central Excise Rules, 1944 were substituted by five set of new rules. As a result of which a new set of CENVAT Credit Rules, 2001 were issued vide Notification No. 31/2001-CE (NT) dt. 21.6.01 (w.e.f. 1.7.01) these rules have replaced the then existing Central Excise Rules, 1944 which were again substituted by CENVAT Credit Rules, 2002 issued vide Notification No.5/2002 - CE (N.T.) dated 1.3.2002 substituting CENVAT Credit Rules, 2001. Recently, these Rules have again been substituted by new CENVAT Credit Rules, 2004 vide Notification No. 23/2004-CE(N.T.) dated September 10, 2004.

CENVAT CREDIT RULES, 2004

The CENVAT Credit Rules, 2004 have replaced the existing Cenvat Credit Rules, 2002 and Service tax Credit Rules, 2002 with effect from 10th September 2004. The new Rules integrated services with goods. With the introduction of these rules, inter sectoral credit is allowed to be taken. Service tax paid on input service is allowed to be used for the duty payable on final products removed. Similarly, excise duty paid on inputs is allowed to be used for paying service tax on output service. Under the new rules, new concepts like input service distributor has been introduced and the definition of capital goods have been expanded. These rules were introduced to avoid cascading effect of multiple taxation.

CASCADING EFFECT

The cascading effect arises when the output of one becomes the input of another. In sell chain goods pass through various stages like distributor, wholesaler, semi-wholesaler and retailer and tax is charged on selling price for example, A sells goods to B for ₹110 (₹ 100 plus tax of ₹10 @10%) and B sells these goods to C after value addition of ₹40 at a selling price of ₹165 (₹150 plus tax of ₹15 @10%) Similarly C sells goods after value addition of ₹35 at a selling price of ₹220 (₹200 plus tax of ₹20@10%).

In this example it is seen that B is paying tax on ₹ 100 on which A has already paid tax and also paying tax on ₹ 10 which is tax paid by A. Similarly, C is paying tax on ₹ 100 on which A and B have already paid tax and on ₹ 40 on which B has already paid tax and also paying tax on ₹10, ₹15 the taxes paid by A and B respectively. This is termed as cascading effect. This distorts the tax structure as tax burden depends on number of stages through which goods passes.

CONCEPT OF CENVAT CREDIT

When the duty paid inputs (raw-materials, consumable stores, packing material etc.) and capital goods are used in the manufacture of finished goods, the duty paid on such inputs etc., will be allowed to be adjusted against the duty payable on the finished goods manufactured. Tax paid at the input level is allowed to be

used against the tax/duty payable at the output level. This scheme is very much useful to the manufacturers as the burden of tax is reduced since it is paid only on value addition.

Example:

Duty paid on raw plastic for the manufacture of plastic furniture is ₹20,000. The duty payable on the finished goods (plastic furniture) is ₹ 35,000 while paying the duty on plastic furniture; the manufacturer is allowed to deduct the amount already paid on raw plastic. Thus, the net duty payable will be ₹15,000 only. Technically speaking, the manufacturer availed the cenvat credit to the extent of ₹20,000 that he paid on inputs while purchasing the same.

If any machine or other capital item is used in the manufacture of plastic furniture as above, the excise duty paid on such capital item is also allowed as set off provided that no depreciation is being claimed on the excise portion under Section 32 of the Income Tax Act, 1961.

If any tax paid service is used in the manufacture of plastic furniture, the amount of service tax paid is allowed to be deducted from the duty payable on plastic furniture. In the same way, when certain inputs are used in providing output service, the duty paid on inputs is allowed to be deducted from the tax payable on output service.

However, if the final product is not dutiable, i.e. when no duty is payable finally on the final product, or when the output service is not taxable - cenvat credit on the inputs/input service used in the manufacture of such final product or provision of output service - is not allowed because there is no cascading effect involved in it. Export of goods/service as a special case enables the manufacturer to take and avail CENVAT credit though no excise duty/service tax is paid on goods/service exported.

Let's discuss the provisions of Cenvat Credit Rules, 2004 as amended from time to time.

CENVAT CREDIT RULES, 2004

Following are the Cenvat Credit Rule, 2004:

Rule	Content
1.	Short title, extent and commencement
2.	Definitions
3.	CENVAT credit
4.	Conditions for allowing CENVAT credit
5.	Refund of CENVAT credit
5A.	Refund of CENVAT credit to units in specified areas
6.	Obligation of a manufacturer or producer of final products and a provider of output service
7.	Manner of distribution of credit by input service distributor
8.	Storage of input outside the factory of the manufacturer
9.	Documents and accounts
9A.	Information relating to principal inputs

10.	Transfer of CENVAT credit
11.	Transitional provision
12.	Special dispensation in respect of inputs manufactured in factories located in specified areas of North East region, Kutch district of Gujarat, State of Jammu and Kashmir and State of Sikkim
12A.	Procedure and facilities for large taxpayer
12AA.	Power to impose restrictions in certain types of cases
13.	Power of Central Government to notify goods for deemed CENVAT credit
14.	Recovery of CENVAT credit wrongly taken or erroneously refunded
15.	Confiscation and penalty
16.	Supplementary provision

DEFINITIONS (RULE 2)

Definition of important terms such as inputs, capital goods, input services, output services etc. have been incorporated in Rule 2 of Cenvat Credit Rules, 2004.

1. CAPITAL GOODS

Capital goods means:

(A) the following goods, namely:-

- (i) all goods falling under Chapter 82, Chapter 84, Chapter 85, Chapter 90, heading No. 6805 grinding wheels and the like, and parts thereof falling under heading 6804 of the First Schedule to the Excise Tariff Act;
- (ii) pollution control equipment;
- (iii) components, spares and accessories of the goods specified at (i) and (ii);
- (iv) moulds and dies, jigs and fixtures;
- (v) refractories and refractory materials;
- (vi) tubes and pipes and fittings thereof;
- (vii) storage tank, and
- (viii) motor vehicles other than those falling under tariff headings 8702, 8703, 8704, 8711 and their chassis but including dumpers and tippers used-
 - (1) in the factory of the manufacturer of the final products, but does not include any equipment or appliance used in an office; or
 - (1A) outside the factory of the manufacturer of the final products for generation of electricity for captive use within the factory; or
 - (2) for providing output service;

(B) motor vehicle designed for transportation of goods including their chassis registered in the name of the service provider, when used for-

- (i) providing an output service of renting of such motor vehicle; or
- (ii) transportation of inputs and capital goods used for providing an output service; or
- (iii) providing an output service of courier agency

(C) motor vehicle designed to carry passengers including their chassis, registered in the name of the provider of service, when used for providing output service of-

- (i) transportation of passengers; or
- (ii) renting of such motor vehicle; or
- (iii) imparting motor driving skills

(D) Components, spares and accessories of motor vehicles which are capital goods for the assessee.

Analysis: Tariff headings 8702, 8703, 8704, 8711 specify motor vehicles meant for transport of goods or persons as well as motor vehicles which are not capital goods but dumpers and tippers with their chassis and accessories used in the factory of the manufacturer of the final products are capital goods.

Capital goods used outside the factory for electricity generation are also capital goods provided that the electricity is used in the factory. Motor vehicles used by certain service providers are capital goods.

2. EXEMPTED GOODS

Exempted goods means excisable goods which are exempt from the whole of the duty of excise leviable thereon, and includes goods which are chargeable to "Nil" rate of duty goods in respect of which the benefit of an exemption under Notification No. 1/2011-CE, dated the 1st March, 2011 or under entries at serial numbers 67 and 128 of Notification No. 12/2012-CE, dated the 17th March, 2012 is availed.

After the amendments in 2011 and 2012, partly exempted goods under the above notifications also fall under the definition of exempted goods.

3. EXEMPTED SERVICE

Exempted Service means a-

- (1) taxable service which is exempt from the whole of the service tax leviable thereon; or
- (2) service, on which no service tax is leviable under section 66B of the Finance Act; or
- (3) taxable service whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken;

but shall not include a service which is exported in terms of rule 6A of the Service Tax Rules, 1994.

4. FINAL PRODUCTS

"Final products" means excisable goods manufactured or produced from input, or using input service.

5. FIRST STAGE DEALER

"First stage dealer" means (i) a dealer, who purchases the goods directly from the manufacturer under the cover of an invoice issued in terms of the provisions of Central Excise Rules, 2002 or from the depot of the

said manufacturer, or from premises of the consignment agent of the said manufacturer or from any other premises from where the goods are sold by or on behalf of the said manufacturer, under cover of an invoice; or

(ii) An importer who sells goods imported by him under the cover of an invoice on which CENVAT credit may be taken and such invoice shall include an invoice issued from his depot or the premises of his consignment agent.

5. INPUT

Input means—

- (i) all goods used in the factory by the manufacturer of the final product; or
- (ii) any goods including accessories, cleared along with the final product, the value of which is included in the value of the final product and goods used for providing free warranty for final products; or
- (iii) all goods used for generation of electricity or steam for captive use; or
- (iv) all goods used for providing any output service;

but excludes—

- (A) light diesel oil, high speed diesel oil or motor spirit, commonly known as petrol;
- (B) any goods used for -
 - (a) construction or execution of works contract of a building or a civil structure or a part thereof; or
 - (b) laying of foundation or making of structures for support of capital goods,
except for the provision of service portion in the execution of a works contract or construction service as listed under clause (b) of section 66E of the Act;"
- (C) capital goods except when used as parts or components in the manufacture of a final product;
- (D) motor vehicles;
- (E) any goods, such as food items, goods used in a guesthouse, residential colony, club or a recreation facility and clinical establishment, when such goods are used primarily for personal use or consumption of any employee; and
- (F) any goods which have no relationship whatsoever with the manufacture of a final product.

Explanation – For the purpose of this clause, “free warranty” means a warranty provided by the manufacturer, the value of which is included in the price of the final product and is not charged separately from the customer;

Analysis:

- (1) Light diesel oil , high speed diesel and petrol are not at all treated as inputs.
- (2) goods used in construction, works contract or any civil work or laying of foundation are not inputs.
- (3) capital goods can be inputs only when they are used as components or parts in the manufacture of final products.
- (4) motor vehicles in no case are treated as capital goods.
- (5) any goods having no relationship with the manufacture of a final product are not inputs.

6. INPUT SERVICE

“Input service” means any service, -

- (i) used by a provider of output service for providing an output service; or

(ii) used by a manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products up to the place of removal, and includes services used in relation to modernisation, renovation or repairs of a factory, premises of provider of output service or an office relating to such factory or premises, advertisement or sales promotion, market research, storage up to the place of removal, procurement of inputs, accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry, security, business exhibition, legal services, inward transportation of inputs or capital goods and outward transportation up to the place of removal;

but excludes,-

- (A) service portion in the execution of a works contract and construction services including service listed under clause (b) of section 66E of the Finance Act (hereinafter referred as specified services) in so far as they are used for -
 - (a) construction or execution of works contract of a building or a civil structure or a part thereof; or
 - (b) laying of foundation or making of structures for support of capital goods, except for the provision of one or more of the specified services; or
- (B) services provided by way of renting of a motor vehicle, in so far as they relate to a motor vehicle which is not a capital goods; or
- (BA) service of general insurance business, servicing, repair and maintenance , in so far as they relate to a motor vehicle which is not a capital goods, except when used by -
 - (a) a manufacturer of a motor vehicle in respect of a motor vehicle manufactured by such person ; or
 - (b) an insurance company in respect of a motor vehicle insured or reinsured by such person; or";
- (C) such as those provided in relation to outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, membership of a club, health and fitness centre, life insurance, health insurance and travel benefits extended to employees on vacation such as Leave or Home Travel Concession, when such services are used primarily for personal use or consumption of any employee

7. INPUT SERVICE DISTRIBUTOR

"input service distributor" means an office of the manufacturer or producer of final products or provider of output service, which receives invoices issued under rule 4A of the Service Tax Rules, 1994 towards purchases of input services and issues invoice, bill or, as the case may be, challan for the purposes of distributing the credit of service tax paid on the said services to such manufacturer or producer or provider, as the case may be.

8. OUTPUT SERVICE

"Output service" means any service provided by a provider of service located in the taxable territory but shall not include a service,-

- (1) specified in section 66D of the Finance Act; or
- (2) where the whole of service tax is liable to be paid by the recipient of service.'

9. SECOND STAGE DEALER

"Second stage dealer" means a dealer who purchases the goods from a first stage dealer.

DUTIES ON WHICH CREDIT CAN BE TAKEN (RULE 3)

Rule 3(1) gives the list of duties, service tax and cess on inputs, capital goods and input services. These are eligible for credit when paid on inputs/capital goods received in the factory of manufacturer or premises of output service provider or input service received by them.

The following types of duties are specified in respect of which credit can be taken:

- (i) Basic Excise Duty (BED) is levied at the rates specified in the First Schedule to the CETA.
- (ii) Special Excise duty (SED) is levied at the rates specified in the Second Schedule to the CETA.
- (iii) Additional Excise Duty (AED) on textiles articles levied under Additional Duties of Excise (Textile and Textile Articles) Act, 1978
- (iv) Additional Excise Duty (AED) on goods of special importance levied under Additional Duties of Excise (Goods of Special Importance) Act, 1957.
- (v) National Calamity Contingent duty (NCCD) leviable under section 136 of the Finance Act, 2001 on cigarettes and pan masala etc.
- (vi) Additional duty of excise leviable under section 157 of the Finance Act, 2003 for development of tea.
- (vii) Additional duty of excise leviable under section 85 of Finance Act, 2005 as Health cess.
- (viii) Countervailing duty (CVD) leviable under section 3 of the Customs Tariff Act. This duty is levied on imported articles and is equal to the duties of excise if the same article is produced or manufactured in India.

However, the CENVAT credit shall not be allowed in excess of eighty-five per cent. of the additional duty of customs paid under sub-section (1) of section 3 of the Customs Tariff Act, on ships, boats and other floating structures for breaking up falling under tariff item 8908 00 00 of the First Schedule to the Customs Tariff Act.

- (ix) Special CVD also known as SAD (Special additional duty) is payable under Section 3(5) of the Customs Tariff Act at 4%. This is in lieu of sales tax. Only a manufacturer is eligible to take this credit on imported goods. Service provider is not eligible as he has no connection with sales tax.
- (x) Education Cess (EC) and Secondary and Higher Education Cess (SHEC) on excisable goods leviable under section 91 read with section 93 of the Finance (No.2) Act, 2004 and under section 136 read with section 138 of the Finance Act, 2007 respectively.
- (xi) Service tax leviable under section 66B of the Finance Act.
- (xii) Education Cess(EC) and Secondary and Higher Education Cess (SHEC) on taxable services leviable under section 91 read with section 95 of the Finance (No.2) Act, 2004 and leviable under section 136 read with section 140 of the Finance Act, 2007 respectively.

and which are paid on-

- (i) any input or capital goods received in the factory of manufacture of final product or by the provider of output service on or after the 10th day of September, 2004 and
- (ii) any input service received by the manufacturer of final product or by the provider of output services on or after the 10th day of September, 2004, including the said duties, or tax, or cess paid on any input or input service, as the case may be, used in the manufacture of intermediate products, by a

job-worker availing the benefit of exemption specified in the notification No.214/86 and received by the manufacturer for use in, or in relation to, the manufacture of final product, on or after the 10th day of September, 2004.

Explanation.- For the removal of doubts it is clarified that the manufacturer of the final products and the provider of output service shall be allowed CENVAT credit of additional duty leviable under section 3 of the Customs Tariff Act on goods falling under heading 9801 of the First Schedule to the Customs Tariff Act.

CENVAT Credit on inputs lying in stock used in the Final products which cease to be exempted [Rule 3(2)]

The manufacturer or producer of final products shall be allowed to take CENVAT credit of the duty paid on inputs lying in stock or in process or inputs contained in the final products lying in stock on the date on which any goods manufactured by the said manufacturer or producer cease to be exempted goods or any goods become excisable .

CENVAT Credit on inputs lying in stock used in the Final products which cease to be exempted [Rule 3(3)]

A service which ceases to be an exempted service, the provider of the output service shall be allowed to take CENVAT credit of the duty paid on the inputs received on and after the 10th day of September, 2004 and lying in stock on the date on which any service ceases to be an exempted service and used for providing such service.

Utilization of Cenvat Credit [Rule 3(4)]

The Cenvat credit may be utilized for payment of:

- (a) any duty of excise on any final product; or
- (b) an amount equal to CENVAT credit taken on inputs if such inputs are removed as such or after being partially processed; or
- (c) an amount equal to the CENVAT credit taken on capital goods if such capital goods are removed as such; or
- (d) an amount required to be paid where goods processed does not amounts to manufacture under sub rule (2) of rule 16 of Central Excise Rules, 2002; or
- (e) service tax on any output service:

Important Points

1. While paying duty of excise or service tax, as the case may be, the CENVAT credit shall be utilized only to the extent such credit is available on the last day of the month or quarter, as the case may be, for payment of duty or tax relating to that month or the quarter. [First Proviso to Rule 3(4)]

2. CENVAT credit cannot be used for payment of service tax in respect of services where the person liable to pay tax is the service recipient.

Restriction on utilisation of credit for payment of duties [Rule 3(7)(b)]

Cenvat credit in respect of;

- (i) additional duty on Textile Articles

- (ii) the National Calamity Contingent duty
- (iii) the education cess on excisable goods
- (iiia) the Secondary and Higher Education Cess on excisable goods
- (iv) the additional duty leviable under section 3 of the Customs Tariff Act, equivalent to the duty of excise specified under items (i), (ii) and (iii) above;
- (v) the additional duty of excise leviable under section 157 of the Finance Act, 2003 (32 of 2003);
- (vi) the education cess on taxable services and
- (via) the Secondary and Higher Education Cess on taxable services
- (vii) Health Cess.

shall be utilised towards payment of duty of excise or as the case may be, of service tax leviable under the said Act respectively.

Table showing the utilization of Cenvat credit

Credit of	Utilisation for
Basic Excise Duty, Special Excise duty, Goods of Special importance and Service Tax	All except health cess
Additional duty on Textile Articles	Additional duty on Textile Articles
National Calamity Contingent duty	National Calamity Contingent duty
Education cess & SHEC on excisable goods	Education cess & SHEC on excisable goods on taxable services
Additional duty leviable under section 3(5) of the Customs Tariff Act	All except Health Cess and service tax
Additional duty of excise leviable under section 157 of the Finance Act, 2003	Additional duty of excise leviable under section 157 of the Finance Act, 2003
The education cess & SHEC on taxable services	Education cess & SHEC on excisable goods on taxable services
Health Cess	Health Cess

Capital Goods or inputs removed as such [Rule 3(5)]

When inputs or capital goods, on which CENVAT credit has been taken, are removed as such from the factory, or premises of the provider of output service, the manufacturer of the final products or provider of output service, as the case may be, shall pay an amount equal to the credit availed in respect of such inputs or capital goods and such removal shall be made under the cover of an invoice referred to in rule 9.

However, such payment shall not be required to be made where any inputs or capital goods are removed outside the premises of the provider of output service for providing the output service.

It is further provided that payment shall not be required to be made where any inputs are removed outside the factory for providing free warranty for final products.

Capital goods cleared as waste and scrap [Rule 3(5A)]

If the capital goods, on which CENVAT credit has been taken, are removed after being used, whether as capital goods or as scrap or waste, the manufacturer or provider of output services shall pay an amount equal to the CENVAT Credit taken on the said capital goods reduced by the percentage points calculated by straight line method as specified below for each quarter of a year or part thereof from the date of taking the CENVAT Credit, namely:-

(a) For computers and computer peripherals:

for each quarter in the first year	@ 10%
for each quarter in the second year	@ 8%
for each quarter in the third year	@ 5%
for each quarter in the fourth and fifth year	@ 1%

(b) For capital goods, other than computers and computer peripherals @ 2.5% for each quarter:

However, if the amount so calculated is less than the amount equal to the duty leviable on transaction value, the amount to be paid shall be equal to the duty leviable on transaction value.

If the capital goods are cleared as waste and scrap, the manufacturer shall pay an amount equal to the duty leviable on transaction value.

Taken Cenvat credit on input or capital goods written off [Rule 3(5B)]

If the value of any,

- (i) input, or
- (ii) capital goods before being put to use,

on which CENVAT credit has been taken is written off fully or partially or where any provision to write off fully or partially has been made in the books of account then the manufacturer or service provider shall pay an amount equivalent to the CENVAT credit taken in respect of the said input or capital goods.

Remission of duty [Rule 3(5C)]

Where on any goods manufactured or produced by an assessee, the payment of duty is ordered to be remitted under rule 21 of the Central Excise Rules, 2002, the CENVAT credit taken on the inputs used in the manufacture or production of said goods and the CENVAT credit taken on input services used in or in relation to the manufacture or production of said goods shall be reversed.

Explanation 1.- The amount payable under sub-rules (5), (5A), (5B) and (5C), unless specified otherwise, shall be paid by the manufacturer of goods or the provider of output service by debiting the CENVAT credit or otherwise on or before the 5th day of the following month except for the month of March, where such payment shall be made on or before the 31st day of the month of March.

Explanation 2.- If the manufacturer of goods or the provider of output service fails to pay the amount payable under sub-rules (5), (5A), (5B) and (5C), it shall be recovered, in the manner as provided in rule 14, for recovery of CENVAT credit wrongly taken and utilised.

Reversal of duty is considered as payment of duty [Rule 3(6)]

The amount of duty written off or reversed under sub-rule (5) or sub rule (5A), shall be eligible as Cenvat Credit as if it was a duty paid.

Credit in respect of goods purchased from 100% EOU [Rule 3(7)(a)]

CENVAT credit in respect of inputs or capital goods produced or manufactured, by a 100% export-oriented undertaking (EOU) or by a unit in an Electronic Hardware Technology Park (EHTP) or in a Software Technology Park (STP) and used

- (i) in the manufacture of the final products or
- (ii) in providing an output service, shall be admissible equivalent to the amount calculated in the following manner

The formula is as follows:

$$\left(1 + \frac{BCD}{200}\right) \times \frac{CVD}{100}$$

Example: Purchased 1,000 units from E.O.U at ₹ 400 (before taxes) BCD 10% and CVD 16%. Find out the Cenvat Credit eligible to the buyer.

Solution:

$$\begin{aligned} \text{Cenvat Credit per unit} &= 400 \left[1 + \frac{10}{200}\right] \times \frac{16}{100} = 400 \left[\frac{210}{200}\right] \times \frac{16}{100} \\ &= ₹ 67.2 \end{aligned}$$

$$\text{for 1,000 units} = 67.2 \times 1,000 = 67,200$$

Alternatively, the CVD amount can be calculated as follows:

	₹
Assessable Value	400
Add: 50% of BCD (i.e. $\frac{1}{2} \times \frac{10}{100} \times 400$)	<u>20</u>
After BCD	<u>420</u>

$$\begin{aligned} \text{CVD on 420 @ 16%} &= \left(420 \times \frac{16}{100}\right) = 67.2 \\ &= 67.2 \times 1,000 \\ \text{for 1000 units} &= 67,200 \end{aligned}$$

N.B. Education cess on CVD is exempt.

Rule 3(7)(c): On imported marble slabs and marble tiles, Cenvat Credit can be taken at a fixed rate of ₹30

per square metre. The Cenvat credit constitutes CVD and special CVD if any.

SUMMARY OF RULE 3: CENVAT CREDIT, UTILIZATION, LIMITATIONS AND CONDITIONS	
RULE 3(1)	<ul style="list-style-type: none"> ◆ Duties & taxes paid on inputs , input service and capital goods ◆ Eligible even on inputs sent for job work ◆ Full credit available on CVD paid on imported project imports. ◆ Only 85% of CVD paid is available as credit on imported ships, boats etc. for breaking.
RULE 3(2)	<p>Manufacturer</p> <p>When exempted goods become dutiable, credit on inventory lying with the manufacturer can be taken</p>
RULE 3(3)	Service provider can also take credit on his inputs if his existing services become taxable.
RULE 3(4)	<ul style="list-style-type: none"> ◆ Various purposes for which CENVAT credit can be utilised. ◆ Utilization of CENVAT credit subject to limitations and restrictions. ◆ Example: Health Cess , Special. CVD, NCCD, Clean Energy Cess.
RULE 3(5)	<ul style="list-style-type: none"> ◆ Removal of inputs and capital goods as such – reverse credit with exact amount of duty paid when brought in. ◆ Relaxations for service provider and manufacturer.
RULE 3(5A)	<ul style="list-style-type: none"> ◆ If cap. Goods other than computers/ computer peripherals, removed after use, avail 2.5% per quarter and part thereof and reverse the balance or amount calculated as per transaction value, whichever is higher.
RULE 3(5B)	If inputs/capital goods are written off fully/partly before use, reverse the credit.
RULE 3(5C)	If remission granted on final products U/ Rule 21, CER, 2002, reverse the credit taken on inputs.
RULE 3(6)	The buyer will get credit on the goods as the duty specified in the invoice.
RULE 3(7)(a)	EOU gets concession of duty on Basic Custom Duty payable on its DTA clearances in specified cases.
RULE 3(7)(b)	Matching/ interchangeability of duties and taxes. Example: Health cess cannot be met from any duty/ tax except health cess itself. NCCD paid alone can be utilized for NCCD payable on mobiles. Clean energy cess shall be paid in cash only.
RULE 3(7)(c)	Special case: Credit @ 30/ per sq. metre on imported marble slabs and tiles.

CONDITIONS FOR ALLOWING CREDIT (RULE 4)

Credit on input [Rule 4(1)]

The CENVAT credit user is allowed to take 100% credit on inputs immediately on bringing them into the factory. Obviously, it can be utilised immediately for duty on any other final product or output service.

The CENVAT credit in respect of inputs may be taken by the provider of output service when the inputs are delivered to such provider, subject to maintenance of documentary evidence of delivery and location of the inputs.

Credit on capital goods [Rule 4(2)]

As per Rule 4(2)(a), in case of capital goods brought into the factory in the premises of the provider of output services or outside the factory of the manufacturer of the final products for generation of electricity for captive use within the factory only 50% is allowed in the financial year of purchase and the rest in the subsequent financial year. However, 100% credit is allowed on capital goods in the following 3 cases:

1. If the capital goods are cleared as such in the same financial year, full credit can be taken on removal.
2. Special CVD paid by a manufacturer on imported capital goods.
3. SSI units.

The CENVAT credit of the additional duty leviable under sub-section (5) of section 3 of the Customs Tariff Act, in respect of capital goods shall be allowed immediately on receipt of the capital goods in the factory of a manufacturer.

But such capital goods must be in possession in the subsequent financial years. This has an exception:

Spares, components, accessories, refractories, moulds, dies and specified goods falling under Chapter 68 need not be in possession in the subsequent financial year. CENVAT credit can be taken even if they are consumed in the first year itself. **[Rule 4(2)(b)]**

CENVAT credit can be taken on capital goods even if they are acquired on lease, hire purchase or loan arrangement. It is therefore not necessary that the goods must be purchased. **[Rule 4(3)]**

Depreciation under Section 32 of Income Tax Act, 1961 shall not be claimed on excise duty portion in the event of availing CENVAT credit on capital goods. **[Rule 4(4)]**

The CENVAT credit user can take credit on inputs sent to job worker for further processing/repair, reconditioning. But he has to reverse/pay the credit amount if the goods are not received back from the job worker within 180 days of sending. It means, he can enjoy the credit upto 180 days only. Beyond that he has to forgo the benefit till he actually receives them back from the job worker. Credit is also allowed in respect of jigs, fixtures moulds and dies sent to job worker. **[Rule 4(5)]**

Goods may also be allowed to be removed from the premises of job worker by taking permission from the Assistant Commissioner. Such an order permitting the removal by the A/C is valid for a financial year. Such an order may specify the conditions for the removal. **[Rule 4(6)]**

The CENVAT credit in respect of capital goods may be taken by the provider of output service when the capital goods are delivered to such provider, subject to maintenance of documentary evidence of delivery and location of the capital goods.

Conditions for Availing Credit on input service [Rule 4(7)]

Cenvat credit in respect of input service is allowed on or after receiving the invoice, bill or challan.

Proviso 1: Where service receiver is liable to pay service tax directly under reverse charge, he is eligible to take credit only after payment of service charge and service tax.

Proviso 2: If the beneficiary of cenvat credit (manufacturer or service provider) does not pay the service charge and the service tax within 3 months of the date of invoice etc, he has to pay/ reverse the credit taken on the basis of the documents received. He becomes eligible to take credit only after the payment of the said amounts. The availing of the credit is subject to other provisions of the Rules.

Proviso 3: The beneficiary of cenvat credit is also required to pay/ reverse the credit to the extent of refund or credit note received from the provider of output service.

Proviso 4: For the documents received before 1st April, 2011, the beneficiary is entitled to credit only after the required payment is made.

Explanation I: The beneficiary can normally make the payment by utilizing (debiting) the existing cenvat credit balance or by availing the payment schedule given under Rule 8 of Central Excise Rules, 2002 or Rule 6 of Service Tax Rules, 1994.

Explanation II: Non-payment is recoverable under Rule 14 of these Rules.

REFUND OF CENVAT CREDIT (RULE 5)

This is a special case of cash refund of unutilised CENVAT Credit. The basic rule is CENVAT credit once taken can only be utilized and no cash refund is allowed.

Example: *A manufacturer paid ₹10,000 duty on inputs purchased and he took credit of the same. He was not able to utilize the credit. Can he claim it as cash refund from the department? The answer is No, but there is an exception under Rule 5 that is - export under bond/letter of undertaking.*

Under Rule 19 of Central Excise Rules, export of final products is allowed without payment of duty when the exporter submits a bond or letter of undertaking (LUT) as the case may be. The manufacturer-exporter can submit LUT, whereas, the merchant exporter has to submit a bond.

The procedure, limitations and conditions have been specified in Notification 42/2001 under this, when duty paid inputs/tax paid input services are used in the manufacture of goods exported under bond/LUT, the exporter has the option to utilise that credit for any goods removed for consumption in India by way of sale or otherwise or it can be utilised for payment of output service tax.

Alternatively, it can be used for paying excise duty on goods exported.

Note: Under Rule 18 of Central Excise Rules, 2002, the exporter has the facility to pay duty on exported goods and claim the amount as rebate.

- Refund is governed by Section 11B of Central Excise Act, 1944. However, this refund is not subject to the scrutiny of doctrine of unjust enrichment.
- There is no eligibility for cash refund where the manufacturer avails rebate under Rule 18 of Central Excise Rules or duty drawback under Section 75 of the Customs Act, 1962.
- Cash refund is subject to conditions and limitations that may be imposed by Central Government by a Notification.
- Deemed exports, viz. clearances from DTA to EOU are also regarded as export, provided such clearances are made without payment of duty under bond or letter of undertaking.

As per Notification No. 27/2012-C.E. (NT.), dated 18-6-2012, refund claim is to be filed quarterly. A person exporting goods and service simultaneously, may submit two refund claims one in respect of goods exported and other in respect of the export of services every quarter.

Determination of refund: The refund shall be determined by the following formula:

Maximum Refund amount that is admissible =

$$\frac{(\text{Export Turnover of goods} + \text{Export turnover of services})}{\text{Total Turnover}} \times \text{Net CENVAT Credit}$$

where, the terms used are defined below:

- (a) **Net CENVAT credit** = CENVAT credit availed on inputs and input services by the manufacturer or the output service provider - Amount reversed in terms of Rule 3(5C) during quarter ;
- (b) **Export turnover of goods** = Value of final products and intermediate products cleared during quarter and exported without payment of duty under bond or letter of undertaking;
- (c) **Export turnover of services** = Payments received during the quarter for export services + Export services whose provision has been completed for which payment had been received in advance in any period prior to the quarter - Advances received for export services for which the provision of service has not been completed during the quarter;
- (d) **Total turnover** = All excisable goods cleared during the quarter including exempted goods, dutiable goods and excisable goods exported + Export turnover of services (as computed above) and value of all other services, during the quarter + All inputs removed as such under Rule 3(5) against an invoice, during the quarter.

Safeguards, conditions and limitations

Notification No. 27 /2012-CE (N.T.) dated, 18th June, 2012 directs that refund of CENVAT credit shall be allowed subject to the procedure, safeguards, conditions and limitations.

Following safeguards, conditions and limitations;

- (a) the manufacturer or provider of output service shall submit not more than one claim of refund under this rule for every quarter:
Provided that a person exporting goods and service simultaneously, may submit two refund claims one in respect of goods exported and other in respect of the export of services every quarter.
- (b) in this notification quarter means a period of three consecutive months with the first quarter beginning from 1st April of every year, second quarter from 1st July, third quarter from 1st October and fourth quarter from 1st January of every year.
- (c) the value of goods cleared for export during the quarter shall be the sum total of all the goods cleared by the exporter for exports during the quarter as per the monthly or quarterly return filed by the claimant.
- (d) the total value of goods cleared during the quarter shall be the sum total of value of all goods cleared by the claimant during the quarter as per the monthly or quarterly return filed by the claimant.
- (e) in respect of the services, for the purpose of computation of total turnover, the value of export services shall be determined in accordance with clause (D) of sub-rule (1) of rule 5 of the said rules.
- (f) for the value of all services other than export during the quarter, the time of provision of services shall be determined as per the provisions of the Point of Taxation Rules, 2011.
- (g) the amount of refund claimed shall not be more than the amount lying in balance at the end of quarter for which refund claim is being made or at the time of filing of the refund claim, whichever is less.

- (h) the amount that is claimed as refund under rule 5 of the said rules shall be debited by the claimant from his CENVAT credit account at the time of making the claim.
- (i) In case the amount of refund sanctioned is less than the amount of refund claimed, then the claimant may take back the credit of the difference between the amount claimed and amount sanctioned.

Procedure for filing the refund claim

- (a) The manufacturer or provider of output service, as the case may be, shall submit an application in Form A annexed to the notification, to the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise, as the case may be, in whose jurisdiction,-
 - (i) the factory from which the final products are exported is situated.
 - (ii) the registered premises of the provider of service from which output services are exported is situated.
 - (a) The application in the Form A along with the documents specified therein and enclosures relating to the quarter for which refund is being claimed shall be filed by the claimant, before the expiry of the period specified in section 11B of the Central Excise Act, 1944 (1 of 1944).
 - (b) The application for the refund should be signed by-
 - (i) the individual or the proprietor in the case of proprietary *firm or karta* in case of Hindu Undivided Family as the case may be;
 - (ii) any partner in case of a partnership firm;
 - (iii) a person authorized by the Board of Directors in case of a limited company;
 - (iv) In other cases, a person authorized to sign the refund application by the entity.
 - (c) The applicant shall file the refund claim along with the copies of bank realization certificate in respect of the services exported.
 - (d) The refund claim shall be accompanied by a certificate in Annexure A-I, duly signed by the auditor (statutory or any other) certifying the correctness of refund claimed in respect of export of services.
 - (e) The Assistant Commissioner or Deputy Commissioner to whom the application for refund is made may call for any document in case he has reason to believe that information provided in the refund claim is incorrect or insufficient and further enquiry needs to be caused before the sanction of refund claim.
 - (f) At the time of sanctioning the refund claim the Assistant Commissioner or Deputy Commissioner shall satisfy himself or herself in respect of the correctness of the claim and the fact that goods cleared for export or services provided have actually been exported and allow the claim of exporter of goods or services in full or part as the case may be.

REFUND OF CENVAT CREDIT TO UNITS IN SPECIFIED AREAS (RULE 5A)

Notwithstanding anything contrary contained in these rules, where a manufacturer has cleared final products in terms of notification of the Government of India in the Ministry of Finance (Department of Revenue) No.20/2007-Central Excise, dated the 25th April, 2007 and is unable to utilize the CENVAT credit of duty taken on inputs required for manufacture of final products specified in the said notification, other than final products which are exempt or subject to nil rate of duty, for payment of duties of excise on said final

products, then the Central Government may allow the refund of such credit subject to such procedure, conditions and limitations, as may be specified by notification.

Explanation: For the purposes of this rule, "duty" means the duties specified in sub-rule (1) of rule 3 of these rules.

CENVAT CREDIT TO SERVICE PROVIDERS PROVIDING SERVICES TAXED ON REVERSE CHARGE BASIS (RULE 5B)

A provider of service providing services notified under sub-section (2) of section 68 of the Finance Act and being unable to utilise the CENVAT credit availed on inputs and input services for payment of service tax on such output services, shall be allowed refund of such unutilised CENVAT credit subject to procedure, safeguards, conditions and limitations, as may be specified by the Board by notification in the Official Gazette.

Safeguards, conditions and limitations

Notification No. 12/2014-CE (N.T.) dated, 3rd March, 2014 directs that refund of CENVAT credit shall be allowed subject to the procedures, safeguards, conditions and limitations.

Following safeguards, conditions and limitations:

- (a) the refund shall be claimed of unutilised CENVAT credit taken on inputs and input services during the half year for which refund is claimed, for providing following output services namely:-
 - (i) renting of a motor vehicle designed to carry passengers on non abated value, to any person who is not engaged in a similar business;
 - (ii) supply of manpower for any purpose or security services; or
 - (iii) service portion in the execution of a works contract;

Explanation:- For the purpose of this notification,-

Unutilised CENVAT credit taken on inputs and input services during the half year for providing partial reverse charge services = (A) – (B)

Where,

$$A = \left(\text{CENVAT credit taken on inputs and input services during the half year} \right) \times \left(\frac{\text{turnover of output service under partial reverse charge during the half year}}{\text{total turnover of goods and services during the half year}} \right)$$

B = Service tax paid by the service provider for such partial reverse charge services during the half year;

- (b) the refund of unutilised CENVAT credit shall not exceed an amount of service tax liability paid or payable by the recipient of service with respect to the partial reverse charge services provided during the period of half year for which refund is claimed;
- (c) the amount claimed as refund shall be debited by the claimant from his CENVAT credit account at the time of making the claim;
- (d) in case the amount of refund sanctioned is less than the amount of refund claimed, then the claimant may take back the credit of the difference between the amount claimed and the amount sanctioned;

- (e) the claimant shall submit not more than one claim of refund under this notification for every half year;
- (f) the refund claim shall be filed after filing of service tax return as prescribed under rule 7 of the Service Tax Rules for the period for which refund is claimed;
- (g) no refund shall be admissible for the CENVAT credit taken on input or input services received prior to the 1st day of July,2012;

Explanation. – For the purposes of this notification, half year means a period of six consecutive months with the first half year beginning from the 1st day of April every year and second half year from the 1st day of October of every year.

Procedure for filing the refund claim

- (a) the provider of output service, shall submit an application in Form A along with the documents and enclosures specified to the jurisdictional Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise, as the case may be, before the expiry of one year from the due date of filing of return for the half year:
Provided that the last date of filing of application in Form A, for the period starting from the 1st day of July,2012 to the 30th day of September,2012, shall be the 30th day of June,2014;
- (b) if more than one return is required to be filed for the half year, then the time limit of one year shall be calculated from the due date of filing of the return for the later period;
- (c) the applicant shall file the refund claim along with copies of the return (s) filed for the half year for which the refund is claimed;
- (d) the Assistant Commissioner or Deputy Commissioner to whom the application for refund is made may call for any document in case he has reason to believe that information provided in the refund claim is incorrect or insufficient and further enquiry needs to be caused before the sanction of refund claim;
- (e) at the time of sanctioning the refund claim, the Assistant Commissioner or Deputy Commissioner shall satisfy himself or herself in respect of the correctness of the refund claim and that the refund claim is complete in every respect;

OBLIGATION OF A MANUFACTURER OR SERVICE PROVIDER (RULE 6)

Rule 6 also deals with the fundamental principle of taking CENVAT credit. No CENVAT credit can be taken on those inputs whose final product is exempt. Similar is the case with services. When the output service is exempt, no input service credit is allowed to be taken. The facility of CENVAT credit in essence is available mainly to remove cascading effect i.e., tax on tax. When the final product or output service is exempt, the input credit is denied. Exempted goods have been defined under Rule 2(d) and Exempted services are also defined under Rule 2(e).

But Rule 6(1) is not absolute. There are several situations providing relaxations. Sub-rule (2) gives one deviation from the above principle.

Rule 6(2) provides that where inputs/input services are used for both taxable and non-taxable goods or services, credit can be taken only on that quantum of inputs used for dutiable goods or taxable services. Separate accounts have to be maintained.

Example: *Leather is used for exempted as well as dutiable footwear, say chappals and shoes. Chappals are exempted and shoes are dutiable. The manufacturer paid the duty of ₹30,000 on leather 60% of leather was*

used for shoes. CENVAT credit can be taken for ₹18,000 (60% of ₹30,000) by maintaining separate accounts.

Rule 6(3) is an extension of Sub-rule (2). It provides for options to the assessee who prefers not to maintain accounts separately.

When no separate accounts are maintained, any one of the 3 options given below shall be availed:

- These options are available to both manufacturers and service providers.
- They can adopt any of them at their convenience.
- The option has to be availed for all the products/ services
- The option shall be carried on till the end of the financial year.

Rule 6(3)(i) : Take full credit but pay 6% on the value of exempted goods/ exempted Services or

Rule 6(3)(ii) : Take full credit and pay back the amount of credit attributable to exempted goods or exempted services by following the procedure specified in Rule 6(3A); or

Rule 6(3)(iii) : Maintain separate accounts for **inputs** and pay the amount on **input services** as per Rule 6(3A) (this is a hybrid system newly introduced, budget 2011)

Proviso 1: If any duty of excise is paid on the exempted goods, the same shall be reduced from the amount payable.

Proviso 2: If any part of the value of a taxable service has been exempted on the condition that no CENVAT credit of inputs and input services, used for providing such taxable service, shall be taken, then the amount shall be six per cent of the value so exempted.

Provided that in case of transportation of goods or passengers by rail, the amount required to be paid under clause (i) shall be an amount equal to 2 per cent. of value of the exempted services.”

PROCEDURE AND CONDITIONS [RULE 6(3A)]

The manufacturer of goods or the provider of output service shall follow the following procedure and conditions are prescribed for determination and payment of amount payable under Rule 6(3)(ii);

- (a) **Intimate to the Superintendent of Central Excise in writing the details of**
 - Name, address and registration no.
 - Date of commencement of the option.
 - Description of dutiable goods/exempted goods or output services/exempted services
 - Cenvat credit lying in balance on the date of exercising the option.
- (b) Determine and pay, provisionally every month the amount of credit attributable to the exempted goods or exempted services.
- (c) Determine finally the amount of Cenvat credit attributable to exempted goods or exempted services for the whole financial year.
- (d) Pay the amount of difference in the provisionally and finally determined Cenvat Credit by 30th June of succeeding financial year.
- (e) If the difference amount is paid beyond 30th June, pay with interest @ 24% per annum for the period after June 30.

- (f) If the amount paid is in excess of what is payable, self adjustment can be made.
- (g) Intimate to the jurisdictional Superintendent of Central Excise within 15 days of payment or adjustment with the details.

Important Note: No credit is allowed on those inputs and input services which are used **exclusively** for exempted goods or exempted services.

Availment of Cenvat Credit in case of Banking Company and NBFC [Rule 6(3B)]

Notwithstanding anything contained in sub-rules (1), (2) and (3), a banking company and a financial institution including a non-banking financial company, engaged in providing services by way of extending deposits, loans or advances, shall pay for every month an amount equal to fifty per cent. of the CENVAT credit availed on inputs and input services in that month.

As per Rule 6(4), If **capital goods** are exclusively used for exempted goods or exempted services, Cenvat credit on duty paid on such capital goods can not be taken. SSI units are an exception.

Note: If capital goods are partly used for exempted goods or exempted services, full credit on them can still be taken.

Rule 6(5): Omitted

Rule 6(6): All clearances made to an EOU, SEZ unit or SEZ developer, EHTP, STP, UN agencies or supplied **for the use of foreign diplomatic missions, diplomatic agents** or an international organisation for their official use or supplied to projects funded by them, for exports under bond or removal of gold or silver arising in manufacture of copper or zinc by smelting and “supplies made for setting up of solar power generation projects or facilities”;

And goods exempt from import duties when supplied against international competitive bidding or supplied to solar power projects.

Although no duty is payable on their clearances as above, input level credit can be taken and no reversal is necessary.

Rule 6(7): The provisions of sub-rules (1), (2), (3) and (4) shall not be applicable in case the taxable services are provided, without payment of service tax, to a unit in a Special Economic Zone or to a developer of a Special Economic Zone for their authorised operations or when a service is exported,

Rule 6(8): For the purpose of this rule, a service provided or agreed to be provided shall not be an exempted service when:-

- (a) the service satisfies the conditions specified under rule 6A of the Service Tax Rules, 1994 and the payment for the service is to be received in convertible foreign currency; and
- (b) such payment has not been received for a period of six months or such extended period as maybe allowed from time-to-time by the Reserve Bank of India, from the date of provision.”

MANNER OF DISTRIBUTION OF CREDIT BY INPUT SERVICE DISTRIBUTOR (RULE 7)

This is entirely a new concept imported into the rules. Earlier there was no provision for input service distributor. Who is an input service distributor? It has been defined under Rule 2(m). They are offices of the manufacturers etc. in many cases, various input services are consumed in the head quarters/administrative offices of manufacturers and output service providers. In such a case, the invoices indicating the payment of service tax will be in the name of such headquarters/administrative offices. A provision has been made for availing credit of such service tax, in the premises where the output services are rendered. Such

headquarters/administrative offices are described as input service distributor (ISD). The ISD under these rules can *distribute* the total amount of service tax paid by it to its various manufacturing or service providing premises.

The input service distributor who pays service tax on input services can distribute the credit to its constituent units subject to the following conditions:

- (a) The credit distributed shall not exceed the amount of service tax paid.
- (b) Credit of service tax attributable to service used by one or more units exclusively engaged in manufacturing of exempted goods/providing exempted services shall not be distributed.
- (c) Credit of service tax attributable to services used wholly by a unit shall be distributed only to that unit. And
- (d) credit of service tax attributable to service used by more than one unit shall be distributed *pro rata* on the basis of the turnover of such unit during the relevant period to the total turnover of all its units, which are operational in the current year, during the said relevant period.

Important Points:

For the purposes of this rule, the 'relevant period' shall be,-

- (a) If the assessee has turnover in the 'financial year' preceding to the year during which credit is to be distributed for month or quarter, as the case may be, the said financial year; or
- (b) If the assessee does not have turnover for some or all the units in the preceding financial year, the last quarter for which details of turnover of all the units are available, previous to the month or quarter for which credit is to be distributed.

DISTRIBUTION OF CREDIT ON INPUTS BY THE OFFICE OR ANY OTHER PREMISES OF OUTPUT SERVICE PROVIDER (RULE 7A)

The provider of output service can take credit on inputs or capital goods on the basis of invoice, challan or bill issued by its other office.

The procedure applicable to first stage or second stage dealer is applicable to the provider of output service.
[Effective from 1st March, 2008]

The main differences between Input Service Distributor under Rule7 and input distributor under Rule 7A are:

- The Input Service Distributor may be a manufacturer or service provider whereas input distributor is service provider.
- The Input Service Distributor distributes credit on service tax paid but the input distributor distributes excise duty paid on inputs and capital goods.

STORAGE OF INPUT OUTSIDE THE FACTORY OF THE MANUFACTURER (RULE 8)

Storage of goods outside the factory may be allowed by Additional Commissioner/Deputy Commissioner in exceptional cases subject to certain conditions and limitations.

DOCUMENTS AND ACCOUNTS (RULE 9)

The CENVAT user necessarily has to make sure that he is following the appropriate procedure to avail the CENVAT credit. Though no statutory records have been specified by the rules, the user has to maintain

proper records on his own and justify his actions in times of doubt/objection raised by the department. Important among them being the duty/tax paying document on the strength of which he has to take the credit. Various types of such documents are namely:

- (a) **Invoice** obtained from various sources of local purchase. The local suppliers may include manufacturers, importers, dealers or their depots, branches, agents etc.
- (b) **Supplementary Invoice** issued by the manufacturer or importer of inputs or capital goods or by provider of output service in addition to the invoice on various counts. The amount paid under this is also eligible for taking CENVAT credit but subject to the condition that such issue of supplementary invoice was NOT necessitated by fraud, wilful misstatement, suppression of facts etc. on the part of the Supplier.

Note: Supplementary invoice issued by service provider is also eligible for taking cenvat credit.

- (c) Bill of Entry in case of direct imports.
- (d) Certificate issued by appraiser of Customs in case of imports by post.
- (e) A challan evidencing the payment of service tax by the person liable to pay service tax.
- (f) An Invoice, bill or challan issued by provider of input service.
- (g) An Invoice, bill or challan issued by provider of input service distributor.

Particulars to be mentioned on the invoice for the purpose of CENVAT Credit

According to Rule 9(2) of the CENVAT Credit Rules, all the particulars mentioned in the Central Excise Rules, 2002 should be mentioned on the invoice. However, if an invoice contains details of payment of duty or service tax, description of the goods or taxable service, assessable value, name and address of the factory or warehouse or provider of taxable service and the jurisdictional Deputy Commissioner/Assistant Commissioner of Central Excise is satisfied that the goods or services covered by the said document have been received or accounted for in the books of account of the receiver, he may allow the CENVAT credit.

The assessee was required to take reasonable steps to ensure that duties/taxes for which CENVAT Credit has been availed are paid prior to 01-03-2007. However, this requirement has been dispensed with from the above date.

Requirements relating to maintenance of records

Following records are required to be maintained in context of CENVAT Credit:

Records to be kept by dealer of input goods/capital goods: The CENVAT Credit in respect of first stage dealer or second stage dealer is allowed only if such of first stage dealer or second stage dealer, as the case may be, has maintained records indicating the fact that the input or capital goods were supplied from the stock on which duty was paid by the producer of such input or capital goods and only an amount of such duty on pro rata basis has been indicated in the invoice issued by him. [Rule 9(4)]

Records regarding input/capital goods to be kept by the output service provider: The provider of output service is required to maintain proper records for the receipt, disposal, consumption and inventory of the input and capital goods in which the relevant information regarding the value, duty paid, CENVAT Credit taken and utilised, the person from whom the input or capital goods have been procured is recorded. [Rule 9(5)]

Records regarding input services to be kept by the output service provider: The provider of output

service is required to maintain proper records for the receipt and consumption of the input services in which the relevant information regarding the value, tax paid, CENVAT Credit taken and utilised, the person from whom the input service has been procured is recorded [Rule 9(6)].

Note: The maintenance of proper records becomes absolutely necessary because the burden of proof regarding the admissibility of the CENVAT credit shall lie upon the provider of output service taking such credit.

Returns: Periodical returns on the utilization/transfer of CENVAT credit have to be submitted by various parties as indicated below:

- (i) The manufacturer to file return within 10 days in the following months. The SSI shall file within 10 days of the close of the quarter.
- (ii) The FSD/SSD (dealers) to file within 15 days of the close of the quarter. The return shall be filed electronically.
- (iii) The service provider to file half yearly return by the close of the month.
- (iv) The input service distributor shall file half year return by the last of the month following the half year period.

The returns are to be submitted to the superintendent of Central Excise.

A revised return can be submitted by a service provider/ input distributor within 60 days of submission of the return.

INFORMATION RELATING TO PRINCIPAL INPUTS (RULE 9A)

(1) A manufacturer of final products shall furnish to the Superintendent of Central Excise, annually by 30th April of each Financial Year, a declaration in the Form specified, by a notification, by the Board, in respect of each of the excisable goods manufactured or to be manufactured by him, the principal inputs and the quantity of such principal inputs required for use in the manufacture of unit quantity of such final products:

(2) If a manufacturer of final products intends to make any alteration in the information so furnished under sub-rule (1), he shall furnish information to the Superintendent of Central Excise together with the reasons for such alteration before the proposed change or within 15 days of such change in the Form specified by the Board under sub-rule (1).

(3) A manufacturer of final products shall submit, within ten days from the close of each month, to the Superintendent of Central Excise, a monthly return in the Form specified, by a notification, by the Board, in respect of information regarding the receipt and consumption of each principal inputs with reference to the quantity of final products manufactured by him.

(4) The Central Government may, by notification and subject to such conditions or limitations, as may be specified in such notification, specify manufacturers or class of manufacturers who may not be required to furnish declaration mentioned in sub-rule (1) or monthly return mentioned in sub-rule (3).

(5) Every assessee shall file electronically, the declaration or the return as the case may be specified in this rule.

Explanation: For the purposes of this rule, "principal inputs", means any input which is used in the manufacture of final products where the cost of such input constitutes not less than 10% of the total cost of raw-materials for the manufacture of unit quantity of a given final products.

TRANSFER OF CENVAT CREDIT (RULE 10)

The manufacturer or service provider can transfer the credit taken by him in case of transfer of business by way of sale, lease, merger etc. such a transfer must be supported by physical transfer of goods/assets. This must be done by taking into confidence Additional Commissioner/Deputy Commissioner and on their satisfaction that everything was done properly.

TRANSFER OF CENVAT CREDIT OF SPECIAL CVD (RULE 10A)

(1) Manufacturer having more than one registered premises can transfer the credit taken on Special CVD paid on imported goods to other units quarterly by making entries in the records and Issuing a transfer challan with details. The transferee unit is entitled to take and utilize the credit based on the transfer challan.

This facility is not available to the units enjoying area based exemption under various notifications.

(2) Both transferor and transferee units have to submit monthly returns separately regarding transfer and receipt of such credit.

TRANSITIONAL PROVISIONS (RULE 11)

Credit taken under the old rules can be utilized under the New Rules, 2004. Such utilization is subject to the current rules in operation.

If an SSI unit following Cenvat credit scheme happens to switchover to nil duty scheme under Notification No.8/2003, it has to reverse the credit taken on the inventory lying at the time of switchover. If it does not have the credit balance, it has to pay to that extent. If any amount still lies in the credit after the reversal it will automatically lapse forever [Rule 11(2)].

Similarly, when the goods are exempt fully or absolutely, the manufacturer is required to reverse the credit attributable to inputs etc. lying in stock. Any balance remaining will lapse and it cannot be utilized for any purpose whatsoever [Rule 11(3)]

Service provider is also required to reverse the credit on inputs when his services become fully exempt [RULE 11 (4)]

SPECIAL DISPENSATION TO NORTH EASTERN STATES ETC. (RULE 12)

Certain units in the specified States get preferential treatment. For that purpose various notifications have been issued by the Government of India. These units get the exemption benefit of duty paid on value addition. In fact these units pay duty on their final product by availing the input credit. But they will get the refund of the net amount paid by them on the removal of their final products. This refund is through credit of account current. Yet, it is not treated as exemption for the purpose of CENVAT credit utilization. Consequently, the buyer manufacturer who purchases inputs or capital goods from these units will get CENVAT credit normally as if nothing was exempted.

Special Refund Scheme for the Eligible Units under Rule 12: A new Rule 5A has been inserted in Cenvat Credit Rules, 2004 [Notification No. 24/ 2007 dated 25th April, 2007].

This Rule 5A provides for the mechanism for refund of unutilized Cenvat credit

This is akin to Rule 5 which gives refund of unutilized credit in respect of exports under a bond or a letter of undertaking.

Procedure for Refund of Cenvat Credit

The Government has prescribed the procedure for claiming refund of the unutilised Cenvat Credit.

- (i) The manufacturer has to file a declaration with his AC/DC describing the finished goods, duty rate, manufacturing formula with reference to quantity and quality of the raw materials.
- (ii) A monthly statement by the 7th of the month has to be filed giving details of opening balance, receipts, value, duty, amount of credit taken and quantity of inputs used during the month, final products manufactured, inputs lying in stock, credit utilised and the amount of credit lying in balance.
- (iii) The AC/DC after verification will refund the unutilised credit within three months from the date of receipt.
- (iv) If there is likely to be any delay in granting the refund, the AC can grant 80% of the amount claimed on a provisional basis.

DEEMED CREDIT (RULE 13)

This is an exception to Rule 3, where Government notifies deemed credit, the amount of credit eligible to be taken is as per the rates notified by the Government, not on actual basis. At present deemed credit is not in vogue.

PENAL PROVISIONS (RULES 14 AND 15)

Rules 14 and 15 provide for recovery and penalties for violations under the Rules.

(i) Recovery of Cenvat credit wrongly taken or erroneously taken or erroneously refunded [Rule14]

Where CENVAT credit has been taken and utilized wrongly or has been erroneously refunded, the same shall be recovered from the manufacturer and service provider with interest as per the provisions of recovery of the amount and interest under Central Excise Act / Finance Act, 1994

Important Note: Now the amended Rule 14 clearly mentions that interest is payable with the amount of Cenvat credit only when credit taken has been utilized and therefore, interest is not payable if the credit taken wrongly was not utilized.

(ii) Confiscation and penalty (Rule 15)

If any person, takes or utilizes CENVAT credit in respect of input or capital goods or input services, wrongly or in contravention of any of the provisions of these rules, then, all such goods shall be liable to confiscation and such person, shall be liable to a penalty not exceeding the duty or service tax on such goods or services, as the case may be, or **two thousand rupees, whichever is greater.**

In a case, where the CENVAT credit in respect of input or capital goods or input services has been taken or utilised wrongly **by reason of fraud, collusion or any wilful mis-statement or suppression of facts, or contravention** of any of the provisions of the Excise Act, or of the rules made thereunder **with intent to evade payment of duty**, then, **the manufacturer** shall also be liable to pay penalty in terms of the provisions of section 11AC of the Excise Act.

In a case, where the CENVAT credit in respect of input or capital goods or input services has been taken or utilised wrongly by reason of fraud, collusion or any wilful mis-statement or suppression of facts, or contravention of any of the provisions of these rules or of the Finance Act or of the rules made thereunder

with intent to evade payment of service tax, then, ***the provider of output service*** shall also be liable to pay penalty in terms of the provisions of section 78 of the Act.

GENERAL PENALTY (RULE 15A)

This new rule provides for general penalty upto ₹5,000/-in case of contravention of any of the provisions of the CENVAT Credit Rules for which no specific penal provision exists.

Other Relevant Points under Case Law

Held in *Dai Ichi Karkaria Ltd.*, 1999, S.C. that no co-relation of inputs and final products is necessary. CENVAT credit taken is indefeasible.

CENVAT credit is available even on inputs lost or destroyed during process. But if there is loss or shortage during transit, no CENVAT credit is available on such lost goods as they were not used in the manufacture.

No CENVAT credit is allowed on inputs and capital goods lost during storage as they cannot be said to be used in relation to manufacture [Maruti Udyog Ltd., 2000].

SPECIAL AUDIT IN CASES WHERE CREDIT OF DUTY AVAILED OR UTILISED IS NOT WITHIN THE NORMAL LIMITS, ETC. (SECTION 14AA)

Section 14AA inserted by the Finance Act, 1997 lays down the provisions for special audit in cases where credit of duty availed/utilised is not within the normal limits. This Section reads:

As per section 14AA(1), if the Commissioner of Central Excise has reason to believe that the credit of duty availed of or utilised under the rules made under this Act by a manufacturer of any excisable goods:

- (a) is not within the normal limits having regard to the nature of the excisable goods produced or manufactured, the type of inputs used and other relevant factors, as he may deem appropriate;
- (b) has been availed of or utilised by reason of fraud, collusion or any wilful mis-statement or suppression of facts, he may direct such manufacturer to get the accounts of his factory, office, depot, distributor or any other place, as may be specified by him, audited by a cost accountant nominated by him.

The cost accountant or chartered accountant so nominated shall, within the period specified by the Commissioner of Central Excise, submit a report of such audit duly signed and certified by him to the said Commissioner mentioning therein such other particulars as may be specified (Section 14AA(2)].

The provisions of Sub-section (1) shall have effect notwithstanding that the accounts of the said manufacturer aforesaid have been audited under any other law for the time being in force or otherwise [Section 14AA(3)]

The manufacturer shall be given an opportunity of being heard in respect of any material gathered on the basis of the audit under Sub-section (1) and proposed to be utilised in any proceeding under this Act or rules made thereunder [section 14AA(5)].

CASE STUDIES

1. FLEX ENGINEERING LTD. 2012 – CENVAT CREDIT

The assessee is a manufacturer of packaging machines tailor made to meet the requirements of the customer. These machines are called F & S Machines.

Flexible plastic films are used for testing the F&S machines before delivering the machines to the customers. The marketability of the said machines is dependent on passing the test.

Held that the testing is essential for marketing the machines, and materials used for the testing qualifies for cenvat credit. Hence the material is input under Cenvat Credit Rules. 2004.

2. GNFC LTD. 2012 (H.C)—CENVAT CREDIT ON CYLINDERS:

ISSUE: Whether the empty cylinders used for transportation of chlorine and also for storage within factory are eligible for cenvat credit!

The department contended that these cylinders were used only for transport and not for use in the factory. Hence not eligible.

The assessee argued that the cylinder is used not only for carrying chlorine but also for connecting to the machine which is fed from the cylinder. It is also used for storage within the factory. Therefore, it is an accessory to the machine for production since chlorine is fed from the cylinder directly.

The Ahmedabad High Court held that cylinder is eligible for credit as it has dual purpose of transport and storage tank.

3. REFUND UNDER RULE 5 OF CENVAT CREDIT RULES, 2004: *The Madras High Court held in GTN ENGINEERING LTD. that relevant date for claiming refund under Rule 5 of Cenvat Credit Rules is date of export of goods made.*

4. A.P PAPER MILLS LTD. 2011 (H.C)- (CENVAT CREDIT Available on unutilized chlorine gas)

Facts: The manufacturer is using chlorine gas in cylinders for the manufacture of paper. Some chlorine is left over in the cylinders and he returns them to the suppliers. The department demanded reversal of cenvat credit on the amount attributable to the chlorine returned unused.

Held: No need to reverse the credit.

Reason: The chlorine in the cylinder is not possible to be used in *toto*. Hence it is to be treated as deemed use or deemed process loss.

5. TATA ADVANCED MATERIAL LTD, 2011 (H.C)- [NO REVERSAL Of CENVAT CREDIT on insurance claim]

Facts: The assessee purchased capital goods and used in the manufacture of excisable goods. He claimed Cenvat credit also. After 3 years, the capital goods were destroyed by fire. He got insurance claim including the excise duty paid. The department demanded reversal of Cenvat credit on the ground that the assessee got the double benefit of excise duty paid.

Held: No need to reverse.

Reasons: Reversal arises when the credit is wrongly/ irregularly availed. There is no question of double benefit as the claim was because of insurance premium incurred separately by the assessee.

6. PRIME HEALTH CARE PRODUCTS- 2011 (H.C)- (CENVAT CREDIT Available on bought out tooth brush attached and sold in combo pack)

Facts: The assessee is manufacturing tooth paste. He added bought out tooth brush and sold the combo pack having tooth paste and tooth brush. Obviously, he availed cenvat credit on bought out tooth brush.

Issue: Whether he can avail Cenvat credit on bought out brush when he has not added the cost of brush in the price of the combo pack.

Held: Yes, the bought out tooth brush is an accessory supplied along with the tooth paste and hence it is input as per definition under Rule 2(k) price is the policy of the manufacturer and it has no nexus with the eligibility.

Other Cases:

1. Rajasthan Spinning & Weaving Mills Ltd. S.C. 2010.

The assessee engaged in the manufacture of yarn availed MODVAT (now CENVAT Credit) on "capital goods" in respect of steel plates and M.S. channels used by them for erection of chimney for the diesel generating set.

The Tribunal concluded that since the chimney is used as an accessory to the diesel generating set, and steel plates and M.S. channels were used in the fabrication of chimney therefore, MODVAT (now it is CENVAT credit) on these items could not be denied.

The Supreme Court upheld the decision of the tribunal.

2. Alok Enterprises: 2010 (H.C.) : The issue in this case was whether the process- of purification and filtration done to make the products (hydro chloric acid & sulphuric acid) marketable -is a manufacturing process.

Facts: The assessee was availing MODVAT (Now it is called CENVAT credit) on inputs used for purifying and filtering hydrochloric acid & sulphuric acid to make them marketable.

The department rejected MODVAT on the ground that the said process is not a manufacturing process as the end product after filtration and purification is same with same entry (classification No.)

The tribunal held that the process is a manufacturing process. The tribunal observed that 'it is well settled law that even if the goods belong to same entry, manufacture takes place if new identifiable / marketable goods known in the market emerge due to operation conducted and the nature of technology used is not relevant.

The High Court confirmed the order of tribunal and held that the assessee is entitled to take MODVAT on inputs used in the process.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What are the conditions to be fulfilled for Cenvat credit taken on inputs or capital goods?
2. How much duty is payable by 100% EOU if the goods manufactured by it are removed to DTA?
3. Whether duty under rule 3(5) can be paid after end of the month as per rule 8 of Central excise Rules, 2002.
4. What is the procedure of sending the goods for job work?
5. Whether credit can be taken on inputs/capital goods used in the manufacture of final product which are deemed to be exported and hence exempted?
6. What are the Documents on the basis of which credit can be taken?
7. What are the duties of excise and tax which can be availed under the Cenvat Credit Rules, 2004 and how the credit can be used?

8. Inputs on which credit has been taken, can be removed from the factory only after reversal of credit". Are there any exceptions to this principle?

SUGGESTED READINGS

- (1) Central Excise Manual — R.K. Jain
 - (2) Excise Law Times — Centax Publications Pvt. Ltd.
 - (3) Indirect Tax Laws and Practice — V.S. Datey

CENTRAL EXCISE LAW

PART VI: EXPORT BENEFITS AND PROCEDURES

After completion of this part the student will;

- Be familiar with the export promotion scheme under excise and customs
- Have knowledge of procedural aspects for exports of goods
- Be aware of export procedure followed without payment of duty
- Understand the export procedure claiming rebate of duty

INTRODUCTION

To maximise exports is a universal urge, and no country in the world is perhaps an exception to it. The methods adopted to achieve this are many and varied, and some, at times, even border on the unacceptable, such as the widely frowned upon but often prevalent ones like 'dumping'. If apart from the eastern industrial giant, Japan, even small Asian countries like South Korea, Nationalist China (Taiwan) etc. have succeeded in making it big on the world export scene, it is a tribute not only to their industry but to the able manner in which their Governments have piloted their export drives.

In India, a conscious effort to boost exports was launched only after independence. However, ever since then, it has been a relentless drive, with ever increasing momentum, to forge ahead on the export front. A variety of schemes have been devised and implemented by the Central and State governments separately, and at times together. Fiscal incentives to exports constitute a major thrust in this regard and the Excise and Customs administration, dealing as it does with commodity taxation, naturally plays a very important role in offering such incentives.

CONTRIBUTION OF CUSTOMS TOWARDS PROMOTING EXPORTS

In the context of exports, the approach of Customs is not revenue oriented, and this is explicit from the very fact that the export duties are confined to very few commodities, which in the view of the Government, can maintain their competitiveness in the world market even after bearing the burden of export duties. Today, only 49 items are subjected to export duties. On the other hand, customs plays a major role in regulating and promoting exports. As for regulation, Customs being the exit point, all export consignments are quite closely examined to ensure that standards of quality are maintained, and goods that are exported conform to regulations and are not inimical to India's social economic objectives. As for promotion of exports, the Duty Drawback Scheme under Sections 74 and 75 of the Customs Act extinguishes to a substantial extent, the impact of Customs and Excise duties on the inputs used in the manufacture of export products, thus ensuring their cost/price viability in export markets.

CENTRAL EXCISE AND EXPORTS

The Central Excise Act, 1944, and the Central Excise Rules, 2002, incorporate a variety of schemes, all designed with a single purpose in view. It is that excisable goods which are to be exported should (as far as is possible) not be burdened with excise duties. Relief is given not only in regard to the duty on the goods exported as such, but also from the duties of excise on indigenous inputs used in their manufacture.

At this juncture, it should be noted that all the schemes now to be examined are applicable only to "excisable goods" and hence it should be useful to analyse what constitute "excisable goods".

Excisable Goods

Section 2(d) of the Central Excise Act, 1944, defines “excisable goods” as goods specified in the Schedules to the Central Excise Tariff Act, 1985, “as being subject to duty of Excise”. Now, way back in 1975, Central Excise was converted into a comprehensive levy, through the introduction of a residuary heading in the Tariff then current (Tariff Item 68). While the new Excise Tariff introduced on 28.2.1986 (Schedules to Central Excise Tariff Act, 1985) does not have a corresponding residuary heading for the tariff as a whole, still, the comprehensiveness of the Excise duty continues. This is done through having a very elaborate tariff schedule with separate residuary sub-headings provided wherever necessary. In the result, as of today, “excisable goods” would cover virtually all goods which may be produced or manufactured in India, except those which Article 246 of the Constitution read with the VIIth Schedule specifically exclude from the purview of the Central Government for purposes of levying and collecting excise duties. The goods so excluded are alcoholic liquors for human consumption, opium, Indian hemp and Other narcotic drugs and narcotics. In the result, all goods produced/manufactured in India except those cited above are today ‘excisable goods’ as covered by the Central Excise Act, 1944. The provisions of Excise law pertaining to exports will cover exports of any of them.

TYPES OF EXPORTERS

Exporters can be either (a) Manufacturer Exporters i.e. exporters who manufacture excisable goods in their registered premises and clear the goods for export either directly from the factory or from their bonded warehouse; or (b) Merchant Exporters who are exporters who procure excisable goods manufactured by others and export them. Exports by either type of parties can be made by sea, air or land, rail and also by post parcels.

EXCISE CONCESSIONS FOR EXPORTS

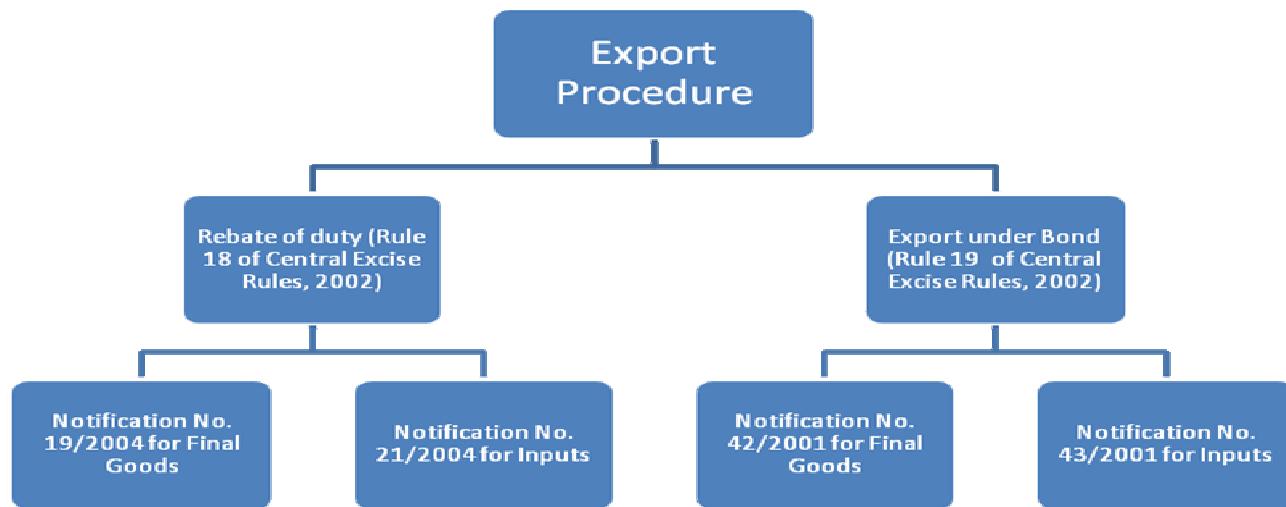
Under the schemes available in the Excise law, the exporter of excisable goods is given the following facilities:

- (i) To export excisable goods on payment of excise duty and to claim refund of such duties subsequent to the export. Such a refund is called rebate.
- (ii) To export the goods without paying excise duty but on the basis of a bond being executed to fulfill the obligation to export.
- (iii) To claim rebate of duty paid on excisable goods used as inputs in the manufacture of goods which are exported.
- (iv) To procure excisable goods required as inputs for manufacture of goods to be exported, without payment of duty on such inputs.

Besides, these concessions, the CENVAT scheme also contains in built provisions to work as a major incentive for production for export. Now let us discuss the provisions of these concessions in detail.

EXPORT PROCEDURES

Excise procedures relating to export promotion schemes have undergone tremendous changes aiming at simplification of the export procedure in *toto*. These export procedures have been made effective from 1.7.2001 by issue of Notifications in this regard. The following chart will give a more clear picture of export procedures:



1. REBATE OF DUTY (RULE 18 OF CENTRAL EXCISE RULES, 2002)

Rule 18 of the Central Excise Rules, 2002 provides where any goods are exported, the Central Government may by Notification grant rebate of duty paid on such excisable goods or duty paid on materials used in the manufacture or processing of such goods and the rebate shall be subject to such conditions or limitations, if any, and fulfilment of such procedures, as may be specified in the notification.

The term "Export" has been defined under Explanation to Rule 18, as per which the term "Export" includes goods shipped as provision or stores for use on board a ship proceeding to a foreign port or supplied to a foreign going aircraft.666

Example:

Wherever excise duty has been paid on export goods or on materials used as inputs for the manufacture of goods exported, rebate (refund) of excise duty paid on such export goods or materials may be granted by Central Govt. by a Notification. For example, item X has been manufactured in India and an excise duty of ₹ 60,000 has been paid. If the same item X is exported, the exporter is entitled to get back ₹ 60,000 as rebate.

(A) Rebate of excise duty paid on export goods is covered under Notification No. 19/2004-Central Excise (NT):

It is specified in this notification that there shall be granted rebate of the whole of the duty paid on all excisable goods falling under the First Schedule to the Central Excise Tariff Act, 1985 (5 of 1986), where the goods are exported to any country other than Bhutan, on fulfillment of the specified conditions, limitations and procedures.

There is no rebate procedure for Bhutan, the rebate to Bhutan was disbursed by the Directorate General of Inspection in accordance with the provisions of the Indo-Bhutan treaty to His Majesty Government of Bhutan. Earlier, separate rebate procedure is followed for Nepal but, in view of the revised Treaty of Trade between India and Nepal rebate export procedure are now at par with exports to other countries.

Rebate is also available on clearance to SEZ vide circular No. 6/2010 – Cus., dated 19-03-2010. However, rebate on exports is not available when manufacturer is availing area based exemption vide Notification No. 37/2007- CE (N.T) dated 17-09-2007.

(1) Conditions and limitations:

The grant of rebate is subject to certain conditions and limitations laid down hereunder:

- (i) The goods shall be exported directly from the factory/warehouse after payment of duty. For the export from any other place, permission through an order from the Board is necessary.
- (ii) The excisable goods shall be exported within six months from the date on which they were cleared for export from the factory of manufacture or warehouse except in cases where the Commissioner of Central Excise extends this limited period, then within such extended period.
- (iii) The quantity of supply as ship stores for consumption to a foreign going vessel shall be determined by the commissioner of customs at the port of shipment.
- (iv) To claim rebate on goods exported to countries like Bhutan and countries other than Bhutan, specified procedure has to be followed.
- (v) If the rebate claim is made by filing electronic declaration, the place of export and date is specified by the Board.
- (vi) The market price of the excisable goods at the time of exportation shall not be less than the rebate claimed.
- (vii) The amount of rebate shall not be less than five hundred rupees.
- (viii) The export goods shall not be the prohibited goods under any law.

(2) Procedure for Claiming Rebate

There are two types of procedures :

- (a) Sealing and endorsement by the Department.
- (b) Self sealing and certification by exporter himself: It may be noted that separate procedure has been set out for exports to Bhutan.
 - The procedure is at two stages;
 - First at the place of removal, i.e. factory, warehouse etc. and

Second at the place of export.

In the first stage, excise department is involved and at the second stage - the customs authorities are involved. Coordination of both the departments is necessary to achieve the object of the scheme.

I. First Stage procedures**A. Sealing and endorsement by the Department**

1. The exporter has to present four copies of application in Form ARE-1 (in addition to the invoice) to the Superintendent or Inspector of excise concerned. The above authority will verify the identity of the goods and the duty particulars. If found in order, he shall seal each package or container in the manner specified by the Commissioner and will endorse each copy of application as a proof of examination.

A.R.E.1 is the export document which shall be prepared in quintuplicate (5 copies). This document shall bear running serial number beginning from the first day of the financial year. The different copies of ARE-1 forms should be of different colors.

2. The Inspector or Superintendent shall deal with the applications in the following manner:

- Return original and duplicate copies of application to the exporter.
- Sends triplicate copy of application by post to the officer with whom rebate claim is to be filed or hands it over to the exporter in a tamper proof sealed cover after posting the particulars in Official records.

Alternatively, sends the triplicate copy of application to the Excise Rebate Audit section at the place of export if rebate is claimed by electronic declaration on Electronic Data Inter-change System of Customs.

3. If the goods are exported by parcel post after the sealing, the exporter has to affix sufficient postage stamps on the duplicate application and submit it along with the parcels.

4. Quintuplicate copy of application may be prepared by the exporter for claiming any other export incentive and shall be dealt in the manner the original application is dealt.

5. In case export of goods is not directly made from the factory of manufacture/warehouse then, the triplicate copy of the application be sent by Superintendent having jurisdiction over the factory of manufacture/warehouse after verification as per aforesaid procedure laid under point No. 2 above.

Distribution of documents (ARE-1)

In the case when export takes place from the factory of warehouse, the distribution of ARE-1 shall be, as follows:

Original (First Copy) and Duplicate (Second Copy)	The Superintendent of Central Excise shall return to the exporter immediately after endorsements and signature.
Triplicate (Third copy)	Sent to the officer with whom rebate claim is to be filed, either by post or handing over to the exporter in a tamper proof sealed cover after posting the particulars in official records.
Quadruplicate (Fourth copy)	Retain for official records
Quintuplicate (Fifth copy)	Optional copy (The Superintendent of Central Excise shall return to the exporter immediately after endorsements and signature)

B. Dispatch of Goods by Self Sealing and Certification by the Exporter

As per these rules, any exporter intending to export any excisable goods can avail the facility of self sealing of export goods. The procedure in brief is as follows:

(1) The owner, the working partner, the managing director or the Company Secretary of the manufacturing unit of the goods or the factory or warehouse or their authorised person, working partner or board of directors of such company, as the case may be, can get the goods sealed and also certify all the copies of the application (ARE-1) that the goods have been sealed in his presence.

(2) On certification - send original and duplicate copies along with the goods to the place of export.

(3) Send triplicate and quadruplicate copies to the Superintendent or Inspector of Excise having jurisdiction over the factory or warehouse concerned within 24 hours of removal of goods.

The exporter shall distribute the copies of ARE 1 in the following manner:

Original (First Copy) and Duplicate (Second Copy)	Send to the place of export along with the goods
TriPLICATE (Third copy) Quadruplicate (Fourth copy)	Sent to the Superintendent of central excise having jurisdiction over the factory or warehouse within 24 hours of removal of the goods.

(4) The officer concerned, after receiving the copies, and verifying the particulars, shall endorse them and send them in the same manner as above to the rebate claims officer/excise rebate audit section, as the case may be.

TriPLICATE (Third copy)	Sent to the officer with whom rebate claim is to be filed, either by post or handing over to the exporter in a tamper proof sealed cover after posting the particulars in official records.
Quadruplicate (Fourth copy)	Retain for official records

(5) The procedure for postal export is same as above.

(6) If the exporter wants to avail any other export incentive, he can submit a quintuplicate copy of application and get it endorsed by both excise and customs officials as above.

(7) In case of export by parcel post, after such goods have been sealed, the exporter is required to affix sufficient postage stamps on the duplicate application so as to cover postal charges and shall present the documents together with the package or packages to which it refers, to the postmaster at the Office of booking.

II. Second Stage Procedures - Examination of Goods at the Place of Export

(1) Excisable goods meant for export shall be presented before the commissioner or duly appointed officer of customs along with original, duplicate and quintuplicate (optional) copies of ARE-1.

(2) The said officer shall examine (physically) the consignment/container vis-a-vis the application in case of self sealing to ensure that the same is correct and exportable under law.

(3) He shall inspect the packages or container if sealed by excise department to ensure that the goods are exportable and the seals are intact.

(4) On satisfaction that everything is in order, the customs officer shall allow export and certify on the copies of applications that the goods have been duly exported and cite the shipping Bill No; date and other particulars of export.

(5) After certification, the original copy is returned to the exporter and duplicate copy is forwarded to the excise officer sanctioning claims or to the Excise Rebate Audit Section, as the case may be.

Alternatively, it may be handed over to the exporter in a tamper proof sealed cover.

(3) Presentation of Claim for Rebate to Central Excise

(i) The exporter can lodge rebate claim from the Assistant Commissioner/ Deputy Commissioner as the case may be, or Maritime Commissioner of Central Excise having jurisdiction over the factory of manufacturer or warehouse by filing the original copy of the application.

(ii) The Assistant/Deputy Commissioner of Central Excise having jurisdiction over the factory of manufacture or warehouse or, as the case may be, Maritime Commissioner of Central Excise shall compare the duplicate copy of application received from the Officer of Customs with the original copy received from the exporter and with the triplicate copy received from the Central Excise Officer and on being satisfied that the claim is in order, sanction the rebate either in whole or in part.

(4) Claim of rebate by electronic declaration

An exporter may enter the requisite information in the shipping bill filed at such place of export, as may be specified by the Board, for claiming rebate by electronic declaration on Electronic Data Inter-change system of Customs. The details of the corresponding application shall be entered in the Electronic Data Inter-change system of Customs upon arrival of the goods in the Customs area. After goods are exported or order under section 51 of the Customs Act, 1962 (52 of 1962) has been issued, the rebate of excise duty shall, if the claim is found in order, be sanctioned and disbursed by the Assistant Commissioner of Customs or the Deputy Commissioner of Customs.

(5) Cancellation of Documents

If the excisable goods are not exported, the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise shall cancel the export documents.

(6) Special Procedure for Stores for Consumption on Board an Aircraft on Foreign Run

In case of mineral products falling under Chapter 27 of the First Schedule to the Central Tariff Act, 1985 exported as stores for consumption on board an aircraft on foreign run, the products as remain on board an aircraft after completion of an internal flight but prior to its reversion to foreign run, the rebate for which shall be granted without production of documents evidencing the payment of duty thereon. The proper officer of customs shall certify in the manner specified by the Commissioner of Central Excise the quantity of products left on board for determining the quantum of rebate thereon.

Explanation I: "duty" means duties of excise collected under the following enactments, namely:

- (a) the Central Excise Act, 1944 (1 of 1944);
- (b) the Additional Duties of Excise (Goods of Special Importance) Act, 1957 (58 of 1957);
- (c) the Additional Duties of Excise (Textiles and Textile Articles) Act, 1978 (40 of 1978);
- (d) the National Calamity Contingent duty leviable under section 136 of the Finance Act, 2001 (14 of 2001), as amended by section 169 of the Finance Act, 2003 (32 of 2003) and further amended by section 3 of the Finance Act, 2004 (13 of 2004);
- (e) special excise duty collected under a Finance Act;
- (f) additional duty of excise as levied under section 157 of the Finance Act, 2003 (32 of 2003);
- (g) Education Cess on excisable goods as levied under clause 81 read with clause 83 of the Finance (No.2) Bill, 2004.
- (h) the additional duty of excise leviable under clause 85 of the Finance Bill, 2005, the clause which has, by virtue of the declaration made in the said Finance Bill under the Provisional Collection of Taxes Act, 1931 (16 of 1931), the force of law."

(i) Secondary and Higher Education Cess on excisable goods leviable under clause (126) read with clause (128) of the Finance Bill, 2007, which has, by virtue of the declaration made in the said Finance Bill under the Provisional Collection of Taxes Act, 1931 (16 of 1931), the force of law

Explanation II: For the purpose of this notification, the expression 'electronic declaration' means the declaration of the particulars relating to the export goods, lodged in the Customs Computer System, through the data-entry facility provided at the Service Centre or the data communication networking facility provided by the Indian Customs and Central Excise Gateway (called ICEGATE), from the computer of the person authorized for this purpose.

Explanation III: For the purposes of this notification, "Maritime Commissioner" means the Commissioner of Central Excise under whose jurisdiction one or more of the port, airport, land customs station or post office of exportation, is located.

(b) Rebate of duty on inputs used in manufacture/processing of export goods (Notification No. 21/2004)

The Government by the Notification allowed rebate of whole of the duty paid on excisable goods, which are in fact materials or inputs for manufacture or processing of other goods, on their exportation out of India, to any country except Bhutan. The amount is paid subject to the conditions and the procedure specified in the above-mentioned notification.

Export goods as per Rule 18 refers to excisable goods (dutiable or exempted) as well as non-excisable goods. Thus, the benefit of input stage rebate can be claimed on export of all finished goods whether excisable or not.

Obviously, when the final products are not dutiable, the rebate can still be claimed on duty paid inputs used in such final products when exported.

Any materials used for manufacture or processing but processing not amounting to manufacture (such as packing, blending etc.) will also be eligible for the benefit under the said notification.

The expression 'material' shall mean all raw materials, consumables, components, semi-finished goods, assemblies, sub-assemblies, intermediate goods, accessories, parts and packing materials required for manufacture or processing of export goods.

However, Rebate of central excise duty paid on equipment and machinery being capital goods used in relation to manufacture or processing of finished goods shall not be allowed.

The benefit of input stage rebate cannot be claimed in any of the following situations:

- (i) where the finished goods are exported under Claim for Duty Drawback;
- (ii) where the finished goods are exported in discharge of export obligations under a Value Based Advance License or a Quantity Based Advance License issued before 31.03.95;
- (iii) where facility of input stage credit is availed under CENVAT Credit Rules, 2004;
- (iv) the market price of the goods is less than the rebate amount;
- (v) the amount of rebate admissible is less than ₹500/-.

The claim for rebate should be filed within the time stipulated under Section 11B of the Central Excise Act, 1944.

Procedures and conditions to be followed

(i) Filing of declaration. - The manufacturer or processor shall file a declaration with the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise having jurisdiction over the factory of manufacture describing;

- the finished goods proposed to be manufactured or processed
- along with their rate of duty leviable and
- Manufacturing/processing formula with particular reference to quantity or proportion in which the materials are actually used as well as the quality.

The declaration shall also contain the tariff classification, rate of duty paid or payable on the materials so used, both in words and figures, in relation to the finished goods to be exported.

Besides the above, the following points are to be observed by the claimant :

- Where there are more than one export product, separate statement of the input-output ratios may be furnished for each export product. The consumption should be net of recycled materials.
- Where recoverable wastages are generated but not recycled but sold on account of its unsuitability, the same should be clearly reflected in the declaration.
- The declarant should also enclose, in case of a new product or in case where the manufacturer is not regularly manufacturing the export goods and clearing for home consumption or export, a write up of manufacturing process.

(ii) Verification and grant of permission

The Deputy/Assistant Commissioner of Central Excise shall verify the correctness of the ratio of input and output mentioned in the declaration filed before commencement of export of such goods, if necessary, by calling for samples of finished goods or by inspecting such goods in the factory of manufacture or process. If, after such verification, the Deputy/Assistant Commissioner of Central Excise is also satisfied that there is no likelihood of evasion of duty, he may grant permission to the applicant for manufacture or processing and export of finished goods.

Clarification: Input output norms notified under the Exim Policy may be accepted by the Department unless there are specific reasons for variation.

Where the input output norms notified under the Exim Policy do not include all the materials used in export goods, the claim under this scheme should not be denied merely on that ground.

If for any reason the Deputy/Assistant Commissioner of Central Excise is not satisfied with reference to the correctness of the consumption norms claimed by the applicant, especially where the product is being manufactured for the first time in his jurisdiction, he may permit the manufacturing operations and the verification of the consumption norms should be completed while the process of manufacture is on. The verification should be completed before allowing the export of the goods. The manufacturer working under this Scheme is to declare the raw materials consumed in the application form 3ARE-2 for claiming rebate.

The permission granted by the Deputy/Assistant Commissioner of Central Excise can be withdrawn at any time if any glaring misuse resulting into loss of revenue comes to his notice.

Any change in the consumption ratio [input-output ratio] should be promptly intimated by the manufacturer to

the Deputy/Assistant Commissioner of Central Excise and the jurisdictional Range Superintendent giving reference of the permission granted. If necessary, the Deputy/Assistant Commissioner of Central Excise may order fresh verification.

(iii) Procurement of material – The manufacturer or processor shall obtain the materials to be utilised in the manufacture of the finished goods intended for export directly from the registered factory in which such goods are produced, accompanied by an invoice under rule 11 of the Central Excise Rules, 2002:

Provided that the manufacturer or processor may procure materials from dealers registered for the purposes of the CENVAT Credit Rules, 2004 under invoices issued by such dealers.

(iv) Removal of materials or partially processed material for processing. – The Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise may permit a manufacturer to remove the materials as such or after the said materials have been partially processed during the course of manufacture or processing of finished goods to a place outside the factory -

- (a) for the purposes of test, repairs, refining, reconditioning or carrying out any other operation necessary for the manufacture of the finished goods and return the same to his factory without payment of duty for further use in the manufacture of finished goods or remove the same without payment of duty in bond for export, provided that the waste, if any, arising in the course of such operation is also returned to the said factory of the manufacture or process; or
- (b) for the purpose of manufacture of intermediate products necessary for the manufacture or processing of finished goods and return the said intermediate products to his factory for further use in the manufacture or process of finished goods without payment of duty or remove the same, without payment of duty for export, provided that the waste, if any, arising in the course of such operation is also returned to the factory of manufacturer or processor;

Any waste arising from the processing of materials may be removed on payment of duty as if such waste is manufactured or processed in the factory of the manufacturer or processor.

(v) Procedure for export – The final goods shall be exported on the application in Form A.R.E. 2 specified in the Annexure to this notification and the procedures specified in Ministry of Finance (Department of Revenue) notification No.19/2004-Central Excise (N.T.), dated the 6th September, 2004. In other words, the exporter has option to pay duty on finished export goods (if these are excisable) and claim rebate of such duty. He may also export the excisable goods without payment of duty. In both cases, fresh A.R.E. 1 is not required because export will be effected on A.R.E. 1 itself. But the procedure specified in the aforementioned notifications relating to removals, distribution of documents at the place of despatch and place of export, acceptance of proof of export/filing of claim etc. shall be followed mutatis mutandis.

(vi) Presentation of claim of rebate. – The claim for rebate of duty paid on materials used in the manufacture or processing of goods shall be lodged only with the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise having jurisdiction of the place approved for manufacture or processing of such export goods.

The following documents shall be presented with the claim :

- (i) Original copy of the ARE-2 form duly endorsed by the Customs Officer;
- (ii) Duly self-attested copy of Shipping Bill (Export Promotion Copy);
- (iii) Duly self-attested copy of Bill of lading/Air way bill;

- (iv) Duplicate copy of the Central Excise Invoice under which Central Excise duty will be paid/accounted as payable on goods cleared for export, [where rebate of finished goods are also being claimed];
- (v) Duplicate copy of the ARE-2 form received from the customs officer in a sealed cover.

(vii) Communication of deficiency in claim

The Assistant Commissioner of Central Excise should point out deficiency, if any within 15 days of lodging of the claim and ask the exporter to rectify the same within 15 days. Queries/deficiencies shall be pointed out at one go and piecemeal queries should be avoided. The claim of rebate should be disposed of within a maximum period of two months.

Only a manufacturer or processor of finished goods who exports the goods can claim benefit of input stage rebate. Benefit of the input stage rebate shall not be extended where export is through merchant exporters.

(viii) Accounts and returns

The manufacturer shall maintain register of duty paid materials brought to the factory for manufacture of finished goods for export under claim for input stage rebate and the account for finished goods manufactured and exported. Any officer duly empowered by the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise in this behalf shall have access at all reasonable times to any premises indicated in the application. The applicant shall also permit the officer of Central Excise to access any records relating to the production, storage and export of goods.

(ix) Checks by customs officers

Samples will be invariably drawn by the Customs Officers for testing at the place of export in case the export goods are of sensitive nature considering that they are made from materials bearing high Central Excise Duty.

Customs officer responsible for making endorsement in A.R.E. 2 shall carefully check that exports are not covered under any of the following :

- (a) The Duty Drawback Scheme;
- (b) A Value Based Advance Licence issued prior to 31.03.95;
- (c) A Quantity Based Advance Licence issued prior to 31.03.95.

2. EXPORT WITHOUT PAYMENT OF DUTY UNDER BOND (RULE 19 OF CENTRAL EXCISE RULES, 2002)

Rule 19 of Central Excise Rules, 2002 specifies that any excisable goods (except wholly exempted or nil rated goods, but including goods cleared by a 100% EOU) may be exported without payment of duty from a factory of the producer or the manufacturer or the warehouse or any other premises as may be approved by the Commissioner.

Any goods for use in the manufacture or processing of goods which are exported may also be removed without payment of duty from a factory of the producer or the manufacturer or the warehouse or any other premises, as may be approved by the Commissioner.

The Export as above shall be subject to such conditions, safeguards and procedure as may be notified by the Board.

Procedures and conditions for export to all countries except Bhutan are specified in notification No. 42/2001-CE(N.T.) dated 26.6.2001. The notification laid down a simplified procedure. The manufacturer-exporter is

not required to submit a bond in Form B-1, an annual letter of undertaking (LUT) UT-1 form is enough. Only a merchant exporter requires to furnish the bond and obtain the CT-1.

(A) Export of excisable goods except to Bhutan without payment of duty (Notification No.42/2001)

1. Conditions: The export shall be subject to the following conditions:

(i) The exporter shall furnish a general bond in the Form B-1 (General Bond- surety/security) to the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise having jurisdiction over the factory, warehouse or such approved premises, as the case may be, or the Maritime Commissioner or such other officer as authorised by the Board on this behalf

- in a sum equal at least to the duty chargeable on the goods,
- with such surety or sufficient security, as such officers may approve
- for the due arrival thereof at the place of export and their export therefrom under Customs or as the case may be postal supervision.

The manufacturer-exporter may furnish a letter of undertaking in FORM UT-1, Letter of Undertaking in lieu of a bond. Hence, merchant exporter has to mandatorily furnish a bond.

(ii) Goods shall be exported within six months from the date on which these were cleared for export from the factory of the production or the manufacture or warehouse or other approved premises within such extended period as the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise or Maritime Commissioner may in any particular case allow.

(iii) When the export is from a place other than registered factory or warehouse, the excisable goods must be in original packed condition and identifiable as to their origin:

(iv) The exports of mineral oil products falling under Chapter 27 of Central Excise Tariff Act, 1985 as store consumption on board of an aircraft on foreign run shall be subject to conditions and limitations, to be applied *mutatis mutandis*, as notified in the Notification No. 40/2001 issued under rule 18 of the said Rules.

(v) Exempted/ Nil rated goods cannot be exported under bond: Goods which are wholly exempted or nil rated other than those cleared by an EOU cannot be exported under the bond scheme.

Forms to be used

ARE-1 form is the export document for export clearance which shall be prepared in quintuplicate (5 copies). This document shall bear running serial number beginning from the first day of the financial year. Certain declarations are required to be given by the exporter on ARE-1 Form.

The exporter or his authorised agent should sign these forms. The different copies of ARE -1 forms should be of different colours

- It will be sufficient if the copies of ARE - 1 form contain a colour band on the top or right hand corner in accordance with above colour scheme.
- An invoice shall also be prepared in terms of rule 11 of the said Rules. It should be prominently mentioned on top "FOR EXPORT WITHOUT PAYMENT OF DUTY".

Letter of undertaking

The Letter of Undertaking is to be furnished in the Form UT-1 specified in Notification No. 42/2001-Central

Excise (N.T.). Any manufacturer, who is an assessee for the purposes of the Central Excise Rules, 2002, shall furnish a Letter of Undertaking only to the Assistant/Deputy Commissioner of Central Excise having jurisdiction over his factory from which he intends to export.

The Letter of Undertaking should not be furnished to the Maritime Commissioner or any other officer. A 'Letter of Undertaking' shall be valid for twelve calendar months provided the exporter complies with the conditions of the Letter of Undertaking, especially the procedure for 'acceptance of proof of export' under this instruction.

In case of persistent defaults or non-compliance causing threat to revenue, the manufacturer-exporter may be asked to furnish bond with security/surety.

This Letter of Undertaking need not be taken for each consignment of export.

If the goods are not exported within six months or such extended period as allowed, the exporter is required to deposit the requisite sum (duty and interest) suo moto, by self-assessment.

Any non-payment within 15 days of expiry of the stipulated time period shall be treated as arrears of revenue and the Department will proceed to recover the same as 'sum due to Government'. Suo motu payment within 15 days of expiry of the stipulated time period will not be treated as 'default'.

On repeated failure of the manufacturer-exporter to comply with the conditions of the Letter of Undertaking or the procedure for 'acceptance of proof of export' under this instruction, the Assistant/Deputy Commissioner of Central Excise may direct him in writing that the letter of undertaking is not valid and he should furnish B-1 Bond with sufficient security/surety.

The Letter of Undertaking shall not be discharged unless the goods are duly exported to the satisfaction of the Assistant/Deputy Commissioner of Central Excise within the time allowed for such export or are otherwise accounted for to the satisfaction of such officer, or until the full duty due upon any deficiency of goods, not so accounted, and interest, if any, has been paid.

Bond by merchant exporter

The merchant-exporters are necessarily required to furnish bond in the B-1 Form with such security or surety as may be specified by the concerned bond accepting authority.

The bond shall be in a sum equal at least to the duty chargeable on the goods for the due arrival of export goods at the place of export and their export there from under Customs or as the case may be postal supervision.

The officer who will accept the bond, will also be responsible for discharging that bond upon furnishing proof of export by the exporter.

The bond shall not be discharged unless the goods are duly exported, to the satisfaction of the Assistant/Deputy Commissioner of Central Excise or Maritime Commissioner or such other officer as may be authorised by the Board in this behalf within the time allowed for such export or are otherwise accounted for to the satisfaction of such officer, or until the full duty due upon any deficiency of goods, not so accounted, and interest, if any, has been paid.

Certificate 'CT-1', shall be obtained by merchant-exporters for procuring goods from a factory or warehouse. Such certificates need not be obtained for each consignment but will be given in a lot of 25.

Bond Accepting Authority

Bond may be accepted by any of the following officers:

- The Assistant/Deputy Commissioner of Central Excise having jurisdiction over the factory or warehouse or any other premises approved by the Commissioner for storing non-duty paid goods.
- Maritime Commissioners at Mumbai, Chennai, Kolkata, Paradeep, Kandla, Tuticorn, Visakhapatnam and Cochin.
- The Assistant/Deputy Commissioner of Central Excise (Export) as officers authorised by the Board for this purpose.

Exporters are required to clearly indicate on the ARE 1 form, the complete postal address of the authority before whom the bond is executed and to whom the documents are to be submitted/transmitted for admission of proof of export.

2. Procedure for removal without payment of duty under this notification

- (i) A Manufacturer-exporter who has furnished a Letter of Undertaking will prepare the export documents (A.R.E.1 and invoice under Rule 11) for clearance from his factory of production.
- (ii) A Merchant-exporter who has furnished a bond shall be provided with sufficient number of certificates (CT-1), duly signed/certified, in multiples of 25 copies. The 'bond accepting authority' shall be responsible for verifying and accepting the proof of export and in case of any defaults by the exporter, to recover the sum and enforcing the bond. The certificate should be provided according to the volume of exports projected by the exporter (which should also reflect in the amount of bond). The compliance of the exporter in submitting the requisite documents towards 'proof of export' shall be another criterion.
- (iii) The second part of CT-1 is very important. The *exporter shall determine* the description of goods for procurement from a particular factory or warehouse or an approved place of storage, quantum, value of procurement (provisional figures) and duty involved therein (provisional figures - but based on correct rate of duty and contracted transaction value). This 'duty' element will be debited provisionally. The exporter shall ensure that at the time of debt sufficient credit is available at that point of time to cover the said debit. The provisional debt shall be converted into final debit within a period of seven days from the date of removal of goods on A.R.E. 1, based on the 'duty payable' on goods cleared for export reflected in the said A.R.E. 1 and invoice.
- (iv) The manufacturer shall record the clearance in his Daily Stock Account indicating *inter alia*, the invoice number/date A.R.E. 1 number/date and duty payable but forgone under Rule 19.

The exporter has two optional procedures regarding the manner in which he may clear the export consignments from the factory or warehouse or any other approved premises namely:

1. Examination and sealing of goods at the place of despatch by a Central Excise Officer.
2. Under self-sealing and self-certification. These were already discussed.

Important note: Goods cleared from DTA to SEZ are eligible for the export benefits under Rule 18/ 19 of Central Excise Rules, 2002.

(3) Export by parcel post

In case of export by parcel post after the goods intended for export has been sealed, the exporter shall affix to the duplicate application sufficient postage stamps to cover postal charges and shall present the

documents, together with the package or packages to which it refers, to the postmaster at the Office of booking.

II. Second Stage Procedure

Examination of goods at the place of export

- (i) The place of export may be a port, airport, Inland Container Depot, Customs Freight Station or Land Customs Station.
- (ii) The exporter shall present together with original, duplicate and quintuplicate (optional) copies of the application (A.R.E. 1) to the Commissioner of Customs or other duly appointed officer - normally goods are presented in the designated export shed.
- (iii) The goods are examined by the Customs for the purposes of Central Excise to establish the identity and quantity, i.e. the goods brought in the Customs area for export on an A.R.E. 1 are the same which were cleared from the factory. The Customs authorities also examine the goods for Customs purposes such as verifying for certain export incentives such as drawback, DEEC, DEPB or for determining exportability of the goods.
- (iv) For Central Excise purposes, the Officers of Customs at the place of export shall examine the consignments with the particulars as cited in the application (A.R.E. 1) and if he finds that the same are correct and the goods are exportable in accordance with the laws for the time being in force (for example, they are not prohibited or restricted from being exported), shall allow export thereof. Thereafter, he will certify on the copies of the A.R.E. 1 that the goods have been duly exported citing the shipping bill number and date and other particulars of export and distribute in the following manner —
- (v) The officer of customs shall return the original and quintuplicate (optional copy for exporter) copies of application to the exporter and forward the duplicate copy of application either by post or by handing over to the exporter in a tamper proof sealed cover to the officer specified in the application, from whom exporter wants to claim rebate.
- (vi) Quintuplicate A.R.E. 1 is the Export Promotion Copy and the exporter shall use this Copy for the purposes of claiming any other export incentive.

Cancellation of applications

- If the excisable goods cleared under A.R.E 1 are not exported for any reason and the exporter intends to divert the goods for home consumption, the following procedure is to be followed.
- He may request in writing the authority who accepted the bond or letter of undertaking to allow cancellation of application, and diversion of goods for consumption in India.
- He shall pay the duty as specified in the application along with interest at the rate of specified in section 11AB on such duty from the date of removal for export from the factory or warehouse or any other approved premises till the date of payment of duty.
- The permission shall be granted within 3 working days. Since duty assessment on A.R.E. 1 has to be done in normal course, there will not be any need for re-assessment by the Department or the assessee unless there are reasons to believe that the assessment was not correct.
- After the duty is discharged, the exporter may take credit in his running bond (where bond is furnished) on the basis of letter of permission, invoice and GAR-7 Challans on which duty is paid. He shall record these facts in the Daily Stock Account.

- If the exporter, after clearing the goods for export without payment of duty, intends to change the destination or buyer or port/place of export, he may do so provided he informs the bond/Letter of Undertaking accepting authority in writing about the changes and makes necessary changes in all the copies of A.R.E.1 and the invoices. If he intends to cancel the original export documents and issue fresh ones, the same may be done under permission and authentication by bond/Letter of Undertaking accepting authority who will ensure that the serial No. and date of the initial documents are endorsed on the fresh documents. In such cases, if bond was furnished for single consignment, fresh bond may not be asked.

1. *Merchant Exporter* mean any exporter who procures and exports excisable goods manufactured by any other person.

2. *"Maritime Commissioner"* means the Commissioner of Central Excise under whose jurisdiction one or more of the port, airport or post office of exportation is located in Mumbai, Kolkata, Chennai, Paradeep, Visakhapatnam, Cochin, Kandla and Tuticorin.

(B) Procurement of Inputs without payment of duty for manufacturing/processing of export goods (Notification No. 43/2001)

- *Raw materials* and other inputs (other than capital goods) are allowed to be procured without payment of excise duty.
- The Board has, by Notification No. 43/2001 -Central Excise (N.T.) dated 26.6.2001 notified the conditions, safeguards and procedures for procurement of the excisable goods without payment of duty for the purpose of use in the manufacture or processing of export goods and their exportation out of India, to any country except Nepal and Bhutan.
- The conditions and procedure for manufacture of export goods in bond shall be as follows:
 - The manufacturer or the processor intending to avail benefit of this notification shall register himself under Rule 9 of the said Rules; and
 - The procedure specified in the Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001 shall be followed, *mutatis mutandis*.
- Other conditions and procedures such as declaration rates and ratios; verification and grant of permission by the Department; removal of materials; disposal and treatment of wastage; application forms [ARE-2] to be used on removal for export; distribution of documents; proof of export; accounts and returns; checks by the customs officer etc. are *almost same* as specified for rebate of duty paid on excisable materials used for the export goods.

Procurement of material

The procedure of procurement of material required for the manufacture shall be governed by the provisions of the Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001.

It may be noted that there is a separate procedure mentioned under the above rules. Under them the manufacturer, procurer of materials at concessional rates/non-payment of duty must

- Get registration under Rule 9;
- Submit an application to the Assistant Commissioner / Deputy Commissioner in the prescribed form;
- Submit a bond to the satisfaction of the authorities;

- Obtain the application certified by the authorities;
- Send the certified copy to the supplier enabling him to remove goods without payment of duty;
- Comply with the post removal procedure (both, the supplier and the procurer).

Only a manufacturer or processor of finished goods who exports the goods can claim benefit of input stage rebate. This facility shall not be extended where exports are through merchant exporters.

OTHER MISCELLANEOUS PROVISIONS

(A) Re-entry of the goods cleared for export under bond but not actually exported, in the factory of manufacture

The excisable goods cleared for export under bond or undertaking but not actually exported for any genuine reasons may be returned to the same factory provided:

- such goods are returned to the factory within six months along with original documents (invoice and A.R.E. 1);
- the assessee shall give intimation of the re-entry of each consignment in Form D-3 within twenty-four hours of such re-entry;
- such goods are to be stored separately at least for 48 hours from the time intimation is furnished to Range Office or shorter period if verification is done by the Superintendent of Central Excise in the manner mentioned subsequently; and
- the assessee shall record details of such goods in DSA and take the stock in the factory.

The Superintendent of Central Excise will verify himself or through Inspector in charge of the factory, about the identity of such goods with reference to invoice, A.R.E. 1 and the daily stock account in respect of 5% of intimations, within another 24 hours of receipt of intimation.

(B) Re-import of exported goods for repairs etc. and subsequent re-export

The exported excisable goods which are re-imported for carrying out repairs re-conditioning, refining, re-making or subject to any similar process may be returned to the factory of manufacture for carrying out the said processes and subsequently re-exported. It may be noted that 're-import and re-export' shall be governed by the provisions of the Customs Act, 1962.

So far Central Excise is concerned, the manufacturer shall maintain separate account for return of such goods in a daily stock account and make suitable entry on the said account after goods are processed, repaired, re-conditioned, refined or re-made. When such goods are exported, the usual export procedure shall be followed.

Any waste or refuse arising as a result of the said processes shall be removed from the factory on payment of appropriate duty or destroyed after informing the proper officer in writing at least 7 days in advance and after observing such conditions and procedure as may be specified by the Commissioner of Central Excise and thereupon the duty payable on such waste or refuse may be remitted by the said Commissioner of Central Excise.

(C) Entry of goods in another factory of the same manufacturer for consolidation and loading of consignment for export

Goods removed without payment of duty for export on A.R.E. 1 from one factory (hereinafter referred to as

'the first factory') of a manufacturer are allowed to enter in another factory of the said manufacturer (hereinafter referred to as the 'subsequent factory') only for the purpose of consolidation and loading of goods manufactured in subsequent factory and export therefrom subject to following conditions:

The exporter shall be required to get his goods examined and sealed at each factory [the place of despatch] by a Central Excise Officer.

The export goods shall be brought under cover of invoice and A.R.E. 1 in the subsequent factory in original packing and duty sealed by Central Excise Officers. In case goods are stuffed in a container, Central Excise Officer shall duly seal the container in the first factory and the sealing of each package shall not be insisted upon. The Central Excise Officer having jurisdiction over the subsequent factory shall supervise the opening of the seal of container, loading of goods (duly sealed if these goods are to be loaded in open truck/vehicle) belonging to the subsequent factory in vehicle or container and sealing of the container.

The exporter or the manufacturer shall pay the supervision charges thereon.

VARIOUS BONDS UNDER EXCISE

A bond is an undertaking given by the assessee to the Govt. assuring the fulfillment of certain obligations. The bonds may be in the nature of surety or security. Various types of bonds are given below:

B-1 BOND: This is a general bond issued for removing goods for exports without payment of duty under Notification NO. 42/ 2001. This can be with surety or security. This is normally submitted by the merchant exporter. The manufacturer exporter need not submit the bond. Instead, he may submit a letter of undertaking in form UT-1

B-2 BOND: This is a general bond issued for provisional assessment. This can be with surety or security. Where an assessee is not able to make final assessment, he may request the A.C./ D.C for provisional assessment under Rule 7 of Central Excise Rules, 2002.

B-3 BOND: Security bond for dispatch of excisable goods removed for re-warehousing and export without payment of duty.

B-8 BOND: This is submitted under CENTRAL EXCISE [Removal Of Goods At Concessional Rate Of Duty For Manufacture of Excisable Goods] RULES, 2001 to procure goods at nil/ concessional rate of duty. Under this scheme, concession of duty is available if the goods are used for intended purpose.

B-11 BOND: This is submitted to get the seized goods released provisionally. This is in the nature of a security bond.. This bond should cover full value of the goods seized. The amount of security, however, is determined by the adjudicating authority. After execution of this bond the seized goods are released. If the goods are confiscated by adjudication order, redemption fine with value of goods is collected from the assessee.

B-17 BOND: This is a general bond submitted by an EOU/ EHTP/ STP units. This may be a surety/ security bond. This is submitted for various purposes; for goods exported without duty, goods procured without payment of duty etc.

SELF - TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What schemes are available in Central Excise under which concessions from levying Central Excise Duties are given for export purposes ?

2. What are the rules and conditions of export of excisable goods under claim for rebate?
 3. Is there any difference between "Manufacturer-Exporters" and "Merchant Exporters" for the purposes of excise concessions on exports? Explain.
 4. What are the rules and procedure of export of goods under Bond?
 5. Is any rebate of duty available to the manufacturer on excisable materials used in the manufacture of goods exported? State the rules in this regard.
 6. What are the various bonds used under Excise?

SUGGESTED READINGS

- (1) Central Excise Manual — *Taxmann*
 - (2) Indirect Taxes Law and Practice — *V.S Datey, Taxmann*

Note: For relevant forms, students may refer to latest edition of Central Excise Manuals..

CENTRAL EXCISE LAW

PART VII: RECOVERY AND REFUNDS OF DUTIES UNDER CENTRAL EXCISE

After completion of this part the students will have the understanding of;

- Procedure for claiming refund
- Interest provisions for delay in refund
- Recovery provisions where duty is not paid in full
- Interest provisions on the amounts due

INTRODUCTION

While excise duties are paid on goods by manufacturers at the time of removal of the goods, it does happen occasionally that the duty so paid is either short or is in excess of the amount which should have actually been paid. Errors of omissions or commissions can arise due to a variety of reasons such as erroneous determination of the rate of duty, or of the assessable value, or wrong quantification of the goods under removal, or even plain arithmetical mistakes in computing the duty to be paid on the consignment under removal. To rectify such errors, the Central Excise Law contains specific provisions, and the Department has prescribed detailed procedures for such purposes.

The errors made in regard to duty might either confer a benefit to Revenue which is not warranted by law, or conversely, might confer an advantage to the assessee which in law is actually not due to him. The errors of the former type can be rectified by the assessee making a claim for refund of duty, whereas the latter type of errors would be set right by the Excise Department demanding and recovering amounts actually due to the exchequer.

Before we go further into refunds and demands, it is note-worthy that it is only amounts which have been paid as duty which can give rise to claims for refund of duty or demands for duty. This would mean that if before filing the return for a particular month, the assessee himself discovers that he has either short paid or excess paid any amount for a particular consignment, he can himself rectify the error by making a suitable credit entry (in the case of excess payment) or a debit entry (in the case of short payment). However, once the return is filed, this facility of the assessee himself correcting errors in payment is restricted to arithmetical errors noticed by the assessing officer only. They can be rectified on suitable directions given by him to the assessee to make appropriate credit or debit entry in his account current [Personal Ledger Account]. In all cases once the return is filed, errors in regard to duties paid can be set right only through refunds/ demands.

Personal Ledger Account (PLA):

Personal Ledger Account is an Account through which Assessee pays duty to the Government. The PLA Register is credited when the duty is liable to pay and when the duty is discharged [By CENVAT CREDIT/PAYMENT] the PLA Register will be debited. The duty payable, if any, will be displayed as balance.

REFUNDS

The situation which creates the need for an assessee claiming a refund of duty are many and varied. The important among them are the following:

- (a) Goods in which no duty is due either due to the goods attracting 'nil' rate under the tariff, or being

totally exempted from duty, being assessed erroneously to duty under an incorrect classification or by denial of an exemption benefit.

- (b) The assessable value having been incorrectly determined the quantum of duty paid being more than what was actually payable.
- (c) Excisable goods cleared on payment of duty for home consumption being ultimately exported from India, and hence actually rendered not liable to duty.
- (d) Accumulation of funds in Account Current which the assessee wants to take out.
- (e) Amounts paid under the Compounded Levy Scheme rates pre-determined, but the rates are subsequently reduced for the period for which duty had been paid at the (pre-reduction) higher rates.
- (f) In cases where duty paid goods are returned to the factory for refining, reconditioning, re-making or for subjecting them to any other similar processes rendering the duty originally paid as refundable.
- (g) refund of duty export rebate scheme.
- (h) refunds arising out of Cenvat Credit Scheme

REFUND OF DUTY (SECTION 11B)

The law relating to refund of excise duty contained in Section 11B of the Central Excise Act, 1944. The definition of refund includes rebate of duty paid on goods exported out of India or on materials used in the manufacture of goods exported out of India. Rebate of excise duty is governed by Rule 18 and 19 of the Central excise Rules, 2002.

Section 11B, makes the following provisions pertaining to claims for refunds of excise duties:

The refund claim of duty and interest can be filed within one year from the relevant date in the specified Form by an assessee or even a person who has borne the duty incidence, to the Deputy/Assistant Commissioner of the Central Excise having a jurisdiction over the factory of manufacture. The limitation of one year does not apply where any duty has been paid under protest.

Relevant date [Explanation to Section 11B(5)] means,

(a) Export of goods: in the case of goods exported out of India where a refund of excise duty paid is available in respect of the goods themselves or, as the case may be, the excisable materials used in the manufacture of such goods, -

- (i) if the goods are exported by sea or air, the date on which the ship or the aircraft in which such goods are loaded, leaves India, or
 - (ii) if the goods are exported by land, the date on which such goods pass the frontier, or
 - (iii) if the goods are exported by post, the date of despatch of goods by the Post Office concerned to a place outside India;
- (b) in the case of goods returned for being remade, refined, reconditioned, or subjected to any other similar process, in any factory, the date of entry into the factory for the purposes aforesaid;
- (c) in the case of goods to which banderols are required to be affixed if removed for home consumption but not so required when exported outside India, if returned to a factory after having been removed from such factory for export out of India, the date of entry into the factory;
- (d) Compounded levy Scheme:** in a case where a manufacturer is required to pay a sum, for a certain

period, on the basis of the rate fixed by the Central Government by notification in the Official Gazette in full discharge of his liability for the duty leviable on his production of certain goods, if after the manufacturer has made the payment on the basis of such rate for any period but before the expiry of that period such rate is reduced, the date of such reduction;

(e) **Non-manufacture:** In the case of a person, other than the manufacturer, the date of purchase of the goods by such person;

(ea) **Goods Exempted:** in the case of goods which are exempt from payment of duty by a special order issued under sub-section (2) of section 5A, the date of issue of such order;

(eb) **Provisional Assessment:** in case where duty of excise is paid provisionally under this Act or the rules made there under, the date of adjustment of duty after the final assessment thereof;

(ec) In case where the duty becomes refundable as a consequence of judgment, decree, order or direction of appellate authority, Appellate Tribunal or any court, the date of such judgment, decree, order or direction;

(f) in any other case, the date of payment of duty.

DOCTRINE OF UNJUST ENRICHMENT

As per section 11B(2), If on receipt of any such application, the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise is satisfied that the whole or any part of the duty of excise and interest, if any, paid on such duty paid by the applicant is refundable, he may make an order accordingly and the amount so determined shall be credited to the Fund (consumer welfare fund created under Section 12C):

Exception to the Doctrine of Unjust Enrichment

However, in the following cases the refund amount instead of being credited to the Fund, be paid to the applicant–

- (a) rebate of duty of excise on excisable goods exported out of India or on excisable materials used in the manufacture of goods which are exported out of India;
- (b) unspent advance deposits lying in balance in the applicant's account current maintained with the Commissioner of Central Excise;
- (c) refund of credit of duty paid on excisable goods used as inputs in accordance with the rules made, or any notification issued, under this Act;
- (d) the duty of excise and interest, if any, paid on such duty paid by the manufacturer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- (e) the duty of excise and interest, if any, paid on such duty borne by the buyer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- (f) the duty of excise and interest, if any, paid on such duty borne by any other such class of applicants as the Central Government may, by notification in the Official Gazette, specify. The central Government shall not issue any notification where the incidence of duty and interest, if any paid on such duty has not been passed on by the persons concerned to any other person.

The Supreme Court in the case of *M/s Mafatlal Industries Ltd. v. Union of India* (per majority of 9 judges Bench) in their judgment dated 19.12.1996 [1997 (89) E.L.T. 247 (SC)] has held that the theory of unjust enrichment is valid and constitutional. However, the theory that the manufacturer would be unjustly impoverished in case of demands has not been agreed to.

The Supreme Court also held in Solar Pesticides case 2000 (116) ELT 401 that refunds will not be allowed on captive consumption of inputs. However, it would be possible to get the refund even in case of captive consumption provided it is proved that the incidence of duty is not passed on to the customers. But there is a necessity for the assessee to prove that the incidence of duty has not been passed on to the customers.

Further, the Supreme Court in the case of CCE v. Allied Photographics 2004 (166) ELT 3 has held that doctrine of unjust enrichment applies even when duty is paid under protest. It has been held that even if there is no change in price before and after assessment (i.e. before and after imposition of duty), it does not lead to the inevitable conclusion that incidence of duty has been passed on to the buyer, as such uniformity may be due to various factors.

There could be situations where the manufacturer has paid the duty and the same has been shown in the invoice issued to the buyer. The buyer failed to reimburse the duty for various reasons. In such case, it would not be proper to conclude that the incidence of the duty has not been passed on to the buyer as the CENVAT credit on inputs/capital goods can be taken based on the duty component mentioned on the invoice and not depending upon the payment to the supplier. Only acceptable evidence would be to show that the buyer has not paid the amount to the manufacturer and has not availed the CENVAT credit of duty paid or if he has taken, he has reversed it.

Refund on the basis of debit note issued by Customer is allowable. Debit note is an enough proof of non transfer of burden [Case Techno Rubber Industries (P) Ltd. 2011 (HC)]

CONSUMER WELFARE FUND (SECTION 12C)

Central Government will establish the fund as prescribed under the rules. The amounts of duty not payable under Sections 11B/ 11C or 11D of Central Excise Act or under Sections 27/ 28A/ 28B of the Customs Act or any income from investments from the fund will be credited to the fund.

UTILISATION OF FUND (SECTION 12D)

The fund so created shall be utilized for the welfare of the consumers as per the rules made by the Govt. Proper records to be maintained as prescribed in this regard.

INTEREST ON DELAYED REFUNDS (SECTION 11BB)

Section 11BB of the Central Excise Act, 1944, provide for payment of interest on refunds of duty which is not paid to the applicant within three months from the date of receipt of application under Sub-section (1) of Section 11B of the Act.

It has also been provided that in cases where appellate remedies are resorted to either by the Department or by the assessees, the refund finally payable shall bear interest for the period starting from the date immediately after the expiry of three months from the date of receipt of applications under Sub-section (1) of Section 11B till the date of refund of duty. It may be specifically noted that:

- (a) interest will be paid only on the amount of duty which is finally held to be refundable.
- (b) the interest will be paid at the rate to be fixed by the Central Government by notification in the Official Gazette as simple interest. The interest shall be paid at The interest rate has been fixed by the CBEC as 6% per annum [Notification No. 67/2003 – C.E. (N.T.) dated 12.9.2003]
- (c) no interest is to be paid on any refunds of fines or penalties; the provision has been made for payment of interest only on delayed refund of duty amounts.
- (d) it is to be clearly noted that interest if any would be payable on the amount of duty to be refunded arising only from proceedings initiated under Section 11B i.e. where an application for refund has been filed.

Interest on delayed refund U/S 11 BB is payable after 3 months of receiving the refund application and not on the date of deposit of duty. *Kanyaka Parameswari Engg. Ltd. and RanBaxy laboratories Ltd. 2011 (S.C.)*

Section 35FF has been added in budget 2008 to the effect that interest on predeposit refund is payable for the delay beyond 3 months if the refund is not made within 3 months.

Note: predeposit becomes refundable by the department where the party wins the appeal.

CASE STUDY

TECHNO RUBBER INDUSTRIES (P) LTD- 2011 (H.C.) – Refund on the basis of debit note allowed:

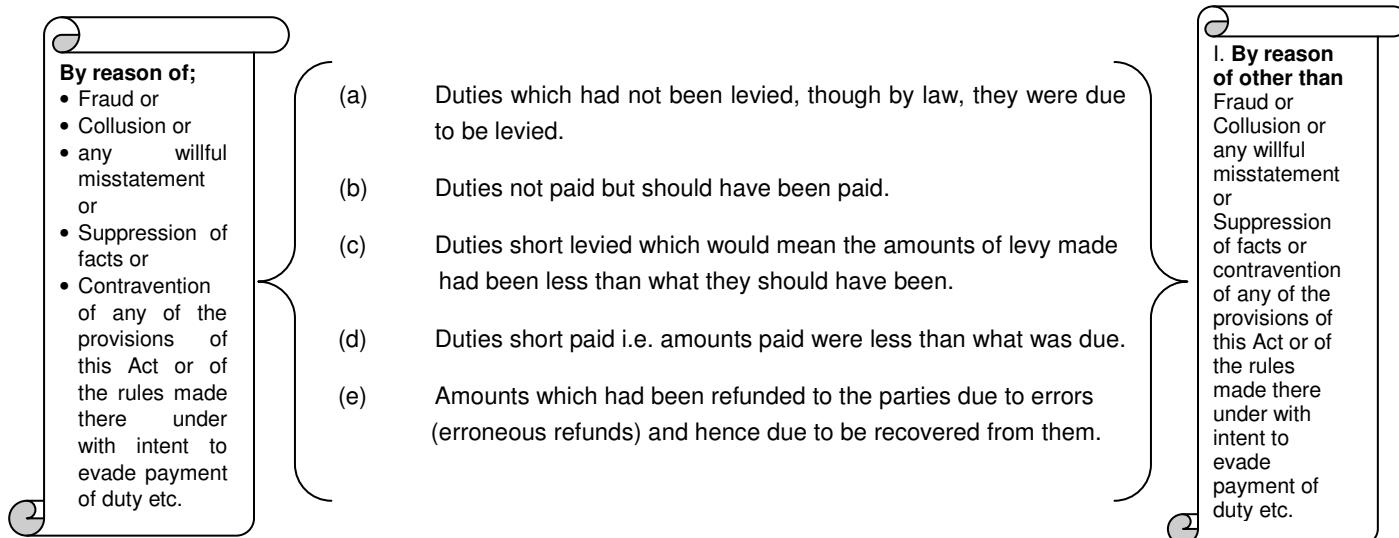
Facts: The assessee paid duty in excess by mistake and charged the same to buyer. But the buyer discovered the excess duty and issued a debit note to the extent charged extra amount.

The assessee filed an application for refund but rejected by department on the contention that the duty was already passed and debit note is not proper proof of not passing on the burden.

Held that debit note is an enough proof of not passing on the burden. The department has to refund the excess amount since it is not tax.

DEMANDS OF DUTY [Section 11A]

The law pertaining to demands by the Department on account of recovery of duties not levied or not paid or short levied or short paid or erroneously refunded, is contained in Section 11A of the Act. Briefly the law authorises the department to demand payment of duty arising in the following situations:



I. Duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, for any reason, other than the reason of fraud or collusion or any wilful misstatement or suppression of facts or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty:

Under Section 11A(1)(a) the Central Excise Officer shall, **within one year from the relevant date**, serve show cause notice on the person chargeable with the duty which has not been so levied or paid or which has been so short-levied or short-paid or to whom the refund has erroneously been made.

Under sub-clause (b), the person chargeable with duty before service of notice under clause (a), may voluntarily

pay duty on the basis of –

- (i) his own ascertainment of such duty; or
- (ii) duty ascertained by the Central Excise Officer, the amount of duty along with interest payable thereon under section 11AA.

As per section, 11A(2), the person who has paid the duty under clause (b) of sub-section (1), shall inform the Central Excise Officer of such payment in writing, who, on receipt of such information, shall not serve any notice under clause (a) of that sub-section in respect of the duty so paid or any penalty leviable under the provisions of this Act or the rules made thereunder.

As per section 11A(3), where the Central Excise Officer is of the opinion that the amount paid under clause (b) of sub-section (1) falls short of the amount actually payable, then, he shall proceed to issue the notice as provided for in clause (a) of that sub-section in respect of such amount which falls short of the amount actually payable in the manner specified under that sub-section and the period of one year shall be computed from the date of receipt of information under sub-section (2).

II. As per section 11A(4), where any duty of excise has not been levied or paid or has been shortlevied or short-paid or erroneously refunded, by the reason of—

- (a) fraud; or
- (b) collusion; or
- (c) any wilful mis-statement; or
- (d) suppression of facts; or
- (e) contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, by any person chargeable with the duty

The Central Excise Officer shall, **within five years from the relevant date**, serve notice on such person requiring him to show cause why he should not pay the amount specified in the notice along with interest payable thereon under section 11AA and a penalty equivalent to the duty specified in the notice.

As per section 11A(5), where, during the course of any audit, investigation or verification, it is found that any duty has not been levied or paid or has been short levied or short-paid or erroneously refunded for the reason mentioned in clause (a) or clause (b) or clause (c) or clause (d) or clause (e) of sub-section (4) but the details relating to the transactions are available in the specified record, then in such cases, the Central Excise Officer shall within a period of five years from the relevant date, serve a notice on the person chargeable with the duty requiring him to show cause why he should not pay the amount specified in the notice along with interest under section 11AA and penalty equivalent to fifty per cent of such duty.

Sub-section (6) of section 11A provides that any person chargeable with duty under sub-section (5), may, before service of show cause notice on him, pay the duty in full or in part, as may be accepted by him along with the interest payable thereon under section 11AA and penalty equal to one per cent of such duty per month to be calculated from the month following the month in which such duty was payable, but not exceeding a maximum of twenty-five per cent of the duty, and inform the Central Excise Officer of such payment in writing.

The Central Excise Officer, on receipt of information under sub-section (6) shall—

- (i) not serve any notice in respect of the amount so paid and all proceedings in respect of the said duty shall be deemed to be concluded where it is found by the Central Excise Officer that the amount of duty, interest and penalty as provided under sub-section (6) has been fully paid;

- (ii) proceed for recovery of such amount if found to be short-paid in the manner specified under sub-section (1) and the period of one year shall be computed from the date of receipt of such information. [Section 11A(7)]

Section 11A(7A): Notwithstanding anything contained in subsections (1), (3), (4) or (5), the CEO may, serve, subsequent to any notice or notices served under any of those sub-sections, as the case may be, a statement, containing the details of duty of central excise not levied or paid or shortlevied or short paid or erroneously refunded for the subsequent period, on the person chargeable to duty of central excise, then service of such statement shall be deemed to be service of notice on such person under the aforesaid subsections, subject to the condition that the grounds relied upon for the subsequent period are the same as are mentioned in the earlier notice or notices. (Finance Act, 2013)

[Section 11A(8)]: Where service of notice is stayed by an order of a court or tribunal, the period of such stay shall be excluded in computing the period of one year referred to in clause (a) of subsection (1) or five years referred to in subsection (4) or (5) as the case may be.

Sub-section 9 of Section 11A provides that where any appellate authority or Tribunal or court concludes that the notice issued under sub-section (4) is not sustainable for the reason that the charges of fraud or collusion or any wilful mis-statement or suppression of facts or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty has not been established against the person to whom the notice was issued, the Central Excise Officer shall determine the duty of excise payable by such person for the period of one year, deeming as if the notice were issued under clause (a) of sub-section (1).

Principles of natural justice: *The Central Excise Officer shall, after allowing the concerned person an opportunity of being heard, and after considering the representation, if any, made by such person, determine the amount of duty of excise due from such person not being in excess of the amount specified in the notice [Section 11A(10)].*

Time-limit for determination of amount of excise duty [Sub-section (11)] *The Central Excise Officer shall determine the amount of duty of excise under sub-section (10)—*

- (a) *within six months from the date of notice in respect of cases falling under subsection (1);*
- (b) *within one year from the date of notice in respect of cases falling under subsection (4) or sub-section (5).*

Order Modified by Appellate Authority [Sub-section (12)]: Where the appellate authority modifies the amount of duty of excise determined by the Central Excise Officer under sub-section (10), then the amount of penalties and interest under this section shall stand modified accordingly, taking into account the amount of duty of excise so modified.

Where the amount as modified by the appellate authority is more than the amount determined under sub-section (10) by the Central Excise Officer, the time within which the interest or penalty is payable under this Act shall be counted from the date of the order of the appellate authority in respect of such increased amount [Sub section 13].

Amount of interest shall be also be paid: Where an order determining the duty of excise is passed by the Central Excise Officer under this section, the person liable to pay the said duty of excise shall pay the amount so determined along with the interest due on such amount whether or not the amount of interest is specified separately (Sub section 14).

Explanation.—For the purposes of this section and section 11AC,—

- (a) “refund” includes rebate of duty of excise on excisable goods exported out of India or on excisable materials used in the manufacture of goods which are exported out of India;

(b) "relevant date" means,—

- (i) in the case of excisable goods on which duty of excise has not been levied or paid or has been short-levied or short-paid, and no periodical return as required by the provisions of this Act has been filed, the last date on which such return is required to be filed under this Act and the rules made thereunder;
- (ii) in the case of excisable goods on which duty of excise has not been levied or paid or has been short-levied or short-paid and the return has been filed on due date, the date on which such return has been filed;
- (iii) in any other case, the date on which duty of excise is required to be paid under this Act or the rules made thereunder;
- (iv) in a case where duty of excise is provisionally assessed under this Act or the rules made thereunder, the date of adjustment of duty after the final assessment thereof;
- (v) in the case of excisable goods on which duty of excise has been erroneously refunded, the date of such refund;

Relevant Date: Relevant date means the date at which the period of limitation starts

If Excise Return was filed (return)	date of filing
If Excise Return was not filed	date on which it should have been filed
If Excise Return is not required to be filed	date of payment of duty
If provisional assessment was done	date of final assessment
If erroneously refunded	date of refund

(c) "specified records" means records including computerised records maintained by the person chargeable with the duty in accordance with any law for the time being in force.'

Clarification on utilization of CENVAT Credit vide Circular No. 962/05/2012-CX dated 28.03.2012

CBEC has clarified that a harmonious reading of rule 8 of the Central Excise Rules, 2002 and first proviso to rule 3(4) of the CENVAT Credit Rules, 2004 indicates that the restriction with regard to the utilization of CENVAT credit is relating to the normal payment of duty in terms of rule 8 of the Central Excise Rules, 2002, where duty for a particular month or quarter is to be discharged by the 5th of the next month or duty paid late in terms of rule 8.

Unlike rule 8 where the duty is paid after self-determination, under section 11A, duty is determined by the Central Excise Officer and the payment is mandated after such determination. Further, there is no time limit prescribed under section 11A i.e., monthly or quarterly unlike the date prescribed under rule 8. Therefore, the restriction on the utilization of the CENVAT credit is not applicable to the demands confirmed under Section 11A of the Central Excise Act, 1944.

Example: Liability to pay duty of ₹2 lac was confirmed for the period of January to March 2011 on a notice issued under Section 11A of the Act. The confirmation order was made on 10th March 2013. The assessee had a Cenvat Credit balance of ₹2,65,000 on 10th March, 2013.

The credit balance can be used for payment of 2 lakh rupees of the past.

INTEREST ON DELAYED PAYMENT OF DUTY (SECTION 11AA)

The provisions relating to interest on delayed payment of duty is contained in section 11AA as follows:

Notwithstanding anything contained in any judgment, decree, order or direction of the Appellate Tribunal or any court or in any other provision of this Act or the rules made thereunder, the person, who is liable to pay duty, shall, in addition to the duty, be liable to pay interest at the rate specified in sub-section (2), whether such payment is made voluntarily or after determination of the amount of duty under section 11A (sub section 1).

Under section 11AA(2), interest, at such rate not below ten per cent and not exceeding thirty-six per cent per annum, as the Central Government may, by notification in the Official Gazette, fix, shall be paid in terms of section 11A after the due date by the person liable to pay duty and such interest shall be calculated from the date on which such duty becomes due up to the date of actual payment of the amount due.

As per Section 11AA(3), no interest shall be payable in the following cases: Notwithstanding anything contained in sub-section (1), no interest shall be payable where,—

- (a) the duty becomes payable consequent to the issue of an order, instruction or direction by the Board under section 37B; and
- (b) such amount of duty is voluntarily paid in full, **within forty-five days** from the date of issue of such order, instruction or direction, without reserving any right to appeal against the said payment at any subsequent stage of such payment.

- *Under section 11AA; interest on duty is charged from the due date*
- *No interest if the demanded duty is paid within 45 days voluntarily without reserving any right to appeal where liability arises due to Board's order/ instruction*
- *A mandatory penalty U/S 11 AC is leviable at 100% or 50% as the case may be, in addition to the duty in case of fraud, willful misstatement ,collusion etc.*
- *But if the assessee pays the amount within 30 days of communication of order determining the amount of duty, only a penalty of 25% of duty amount is payable. This concession is available where the penalty is payable at 50%. The penalty at 50% is payable only in case of recorded transactions. In other cases 100% is payable.*

NOTE: The assessee has to deposit the money first even if he wants to appeal further. The appellate authority may waive it partly or fully on application filed by the party on grounds like—financial stringency and strong case in favour of the assessee.

Interest payable if any shall also to be deposited along with the amount of predeposit of duty.

MODE OF RECOVERY (SECTION 11)

- *Department adjusts the amount payable against the amount refundable, if any.*
- *If necessary, attaches & sells excisable goods.*
- *If necessary, issues a certificate to the District Collector, empowering him to recover as arrears of land revenue.*
- *Excise department also has additional powers to recover the amount under section 142 of The Customs Act.*

PENALTY IN CERTAIN CASES [SECTION 11AC]

- As per Section 11AC(1): (a): If the liability is due to fraud etc, the penalty shall be 100% of duty.
- (b): If the discovery of fraud etc. is on the basis of recorded transactions, the penalty shall be 50% of duty.
- (c): If the amount as above is paid within 30 days of communication of order, the penalty of 50% shall be reduced to 25%.
- (d): If the amount of duty is modified by any appellate authority/court, the amount of penalty also stands modified accordingly.

Section 11AC(2): If the amount so modified increases the liability of the person charged, the amount of interest and penalty on the increased amount shall be calculated from the date of order of such appellate authority.

POWER NOT TO RECOVER DUTY OF EXCISE NOT LEVIED OR SHORT LEVIED AS GENERAL PRACTICE (SECTION 11C)

The need for demanding duty under Section 11A naturally arises due to amounts of duty not being charged or paid correctly. One of the several reasons which can give rise to the original error could be a wrong interpretation of the Central Excise Law, including the tariff and notification. While individual errors of this nature are no doubt rectified through demands under Section 11A, it may occasionally happen that the erroneous interpretation of law conferring the undue benefit to the assessee, was in fact not confined to a few sporadic cases, but the error was fairly widespread. Such an erroneous “general practice”, if it is to be rectified through demands, may not be fair to the industry and trade, particularly since excise is an indirect tax and whatever amounts are paid by the assessee, are passed on and recovered from the consumers. Wherever retrospectively such assessments are re-opened there is an element of inequity in that the assessee have no means of recovering the extra amounts from the market where the goods in question already stand sold. Taking this into consideration, a new provision was introduced on 1.7.1978 as Section 11C.

This section authorises the Central Government not to recover duties, if the amounts in question are due to errors in interpretation of the law which errors were not stray or sporadic, but were ubiquitous, and thus constituted a “general practice”. In such situations, Section 11C authorises the Government to issue a notification in the Gazette directing non-recovery of the sums.

The section clearly meant to provide equitable relief to assessee who had in good faith paid less duty than was legally due. But in the stray cases where duty was fully recovered as due under the law at the time of clearance no refund of duty already paid was permissible. In 1988, the Customs and Central Excises Laws (Amendment) Act, (Act No. 29 of 88) amended Section 11C of Central Excise Act, 1944 (w.e.f. 1st July, 1988) and Sub-section (2) was introduced.

This sub-section empowered refunds being claimed and granted wherever eligible as a consequence of a notification issued under Section 11C(1) subject to the condition that for grant of such refunds the claimant in each such case should prove to the satisfaction of the Assistant Commissioner that the incidence of the duties to be refunded had not been passed on to any other person. The time limit for claiming such refunds is one year.

This section continues to allow such refunds but with the amendment of whole law on refunds, Sub-section (2) of Section 11C has also been amended whereby refunds under this Section would be subject to same provisions as refunds under Section 11B i.e. excess duty would be refunded to the tax payer if he satisfies the prescribed conditions, and otherwise the same will be credited to the Consumer Welfare Fund.

DUTIES COLLECTED FROM BUYER TO BE DEPOSITED WITH THE GOVERNMENT [SECTIONS 11D AND 11DD]

Under Section 11D(1) the assessee who collected the duty in excess of what is required under the law from the buyer, has to deposit the amount with the Department Immediately.

Similarly, every person who collected any amount from any person in excess of any amount representing duty on excisable goods fully exempt or nil rated, shall pay the amount to the govt. immediately. [Section 11D (1A)]

The CEO [Central Excise Officer]may serve the show cause notice for recovery. [Section 11D (2)]

The person has to pay on the demand order passed by the CEO. [Section 11D(3)]

Any surplus amount recovered by the govt. under this is adjustable against the subsequent demand. [Section 11D(4)]

Buyer is entitled to claim refund of the amount of surplus after adjustment under subrule (4), if he makes an application within 6 months of public notice issued by AC for refund. If the amount remains unclaimed, it will be transferred to consumer welfare fund. [Section 11D(5)]

Or else it is payable with *interest @ 15%* under Section 11DD.

The interest is calculated from first date of the following month till the date of payment.

Section 11D(1) covers manufacturers of dutiable goods and Section 11D(1A) refers not only to manufacturers of nil rated and exempted goods but also registered dealers (FSD/ SSD)

PROVISIONAL ATTACHMENT OF PROPERTY IN CASE OF RECOVERY UNDER SECTION 11DDA

The AC/DC may order for provisional attachment of property belonging to the assessee as a precautionary measure after serving an SCN under Section 11A or 11D

- ◆ Such provisional attachment shall be in the prescribed manner.
- ◆ To protect the interest of the Revenue.
- ◆ With prior approval of the Commissioner.
- ◆ Such an attachment can be for a period of six months only.
- ◆ Extension can be granted by chief commissioner by a maximum of 2 years only.

CASE STUDY

HANS STEEL ROLLING MILL 2011 (S.C.): Limitation Period For Recovery- Whether Applicable To Compounded Levy Scheme.

Held: No.

The Supreme Court asserted that general provisions of Section 11A for recovery of amounts due under compounded levy scheme (CLS) are not applicable. CLS is a unique, comprehensive self made scheme. Rules under the scheme specifically stipulate method, manner and time of collection of dues, interest and penalty.

EXCISE AUDIT—2000

In the Budget proposals for the Financial year 1996-97, the Finance Minister announced that a 'scheme of selective audit by the excise officers' in place of the then existing internal audit would be started. Instructions regarding this 'Selective' Audit were later issued by the CBEC in November 1996 vide Circular No. 267/101/96-CX, dated 13.11.1996. This audit was primarily directed at units other than SSI units and medium units paying annual revenue of less than Re. one crore, and it envisaged an in-depth scrutiny of the statutory records and returns.

In October 1999, the Department decided to 'have a more scientific and effective audit system by professionally trained officers', and introduced a 'New Excise Audit System Code' named as 'Excise Audit—2000' (EA-2000). Instructions and guidelines regarding this system were issued by CBEC vide Circular No. 491/57/99-CX, dated 28.10.1999, and No. 514/10/2000-CX, dated 16.2.2000.

As per the details circulated by the Department, the Excise Audit—2000 introduced with effect from 15th November, 1999 have the following main features:

- A minimum of 15 days' notice should be issued to the concerned assessee before commencing any audit.
- The actual audit shall commence w.e.f. 1st December, 1999.
- It is not an Additional Audit but only a modification of existing internal audit system.
- Emphasis under this audit has been made on scrutiny of business records of the company/assessee rather than statutory records.

It is separate from "Special Audit" under Sections 14A and 14AA of the Act.

Excise Audit shall be conducted in respect of units paying duty of ₹ 5 crores and above from the account current in the preceding financial year. Audit of other units will continue to be made as per the existing Audit Manual.

Units already audited in the current financial year under the existing audit system shall continue to be audited as per existing Audit Manual.

It is a Departmental audit conducted by auditors who are excise officers and Assistant Director (Costs) who are Cost Accountants by qualification and are specially trained for this purpose. Assistant Director (Costs) shall conduct this audit in major units.

The main thrusts of Excise Audit are:

- *to improve the present audit system;*
- *adoption of Information Technology in auditing;*
- *preparation of Manpower for Service Tax Audit;*
- *procedural relaxations in excise law;*
- *to provide tools for uniform decision making with the help of Information Technology;*
- *optimal use of manpower in audit.*

This audit shall be conducted with the help of Audit Manual, Standard Audit Programme and Working Papers. The Audit Manuals will lay down audit standards, instructions, policies and procedures relating to audit of an assessee and ensure that audits are uniform, comprehensive and efficient in accordance with the standards laid therein.

Standard audit programme is a systematic and comprehensive sequence outlining the procedure for conduct of audit in order to arrive at an opinion concerning the degree of compliance by the assessee to the law and procedure. And working papers details the work done by the audit party in the given format and shall be filed by the Supervisors of the Audit team. There will be a set of working papers for each item of work/verification done by the auditors.

This audit is required to be completed within 5 to 7 working days. This period may be extended in exceptional cases. To keep the number of days for audit within a reasonable limit, the Commissioner may enhance the strength of the audit team or depute two audit teams clearly specifying its functions.

SPECIAL AUDIT IN CERTAIN CASES (SECTION 14A)

If at any stage of enquiry, investigation or any other proceedings before him, any Central Excise Officer not below the rank of an Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise, having regard to the nature and complexity of the case and the interest of revenue, is of the opinion that the value has not been correctly declared or determined by a manufacturer or any person, he may, with the previous approval of the Chief Commissioner of Central Excise, direct such manufacturer or such person to get the accounts of his factory, office, depots, distributors or any other place, as may be specified by the said Central Excise Officer, audited by a cost accountant or chartered accountant, nominated by the Chief Commissioner of Central Excise in this behalf [Section 14A(1)].

As per section 14A(2), the cost accountant or chartered accountant, so nominated shall, within the period specified by the Central Excise Officer, submit a report of such audit duly signed and certified by him to the said Central Excise Officer mentioning therein such other particulars as may be specified.

The Central Excise Officer may, on an application made to him in this behalf by the manufacturer or the person and for any material and sufficient reason, extend the said period by such further period or periods as he thinks fit; so, however, that the aggregate of the period originally fixed and the period or periods so extended shall not, in any case, exceed one hundred and eighty days from the date on which the direction under sub-section (1) is received by the manufacturer or the person.

These provisions shall also be applicable even if the accounts of the manufacturer or person aforesaid have been audited under any other law for the time being in force or otherwise.

The manufacturer or the person shall be given an opportunity of being heard in respect of any material gathered on the basis of audit under sub-section (1) and proposed to be utilised in any proceedings under this Act or rules made thereunder.

"cost accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 (23 of 1959).

"chartered accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949 (38 of 1949).

Conclusion

While the facilities available in Central Excise for rectification of errors made in assessment of goods are as outlined above, it has to be observed that excise being an indirect tax, any error in assessment, even if it is eventually rectified, creates problems for which there can be no solution. Duties demanded subsequent to the assessment and payment of duty on the consignments, create an unwarranted hardship to the assessee since they have no means of recovering the sums from the market. On the other hand grant of refunds have been made so stringent it cannot reach the assessee or each consumer(s) who has actually borne the duty.

Thus, refunds which earlier allegedly gave rise to undue enrichment of the assessees would most likely keep eluding the consumers also despite there being a specific provision to the effect now made in the law. Since demands and refunds both create consequences not sustainable on grounds of equity, the ideal would be that no occasion should be created for refund claims to arise or for demands to be issued. This would mean that all assessments should always be cent per cent correct. Unfortunately, as with all ideals, this has to remain only an ideal. To err is human, and the assessees as well as the departmental officers are certainly human.

QUICK REFERENCE TABLE

The Refund and Recovery provisions are more or less similar. Therefore, for quick reference the table containing provisions of Customs and Excise is produced here.

SI No.	Provision	Central Excise Section No.	Customs Section No.
1.	Serving of notice	37C	153
2.	Recovery of sums due to government	11	142
3.	Recovery of duties not levied or not paid or short levied or erroneously refunded	11A	28
4.	Interest on delayed payment of duty	11AA	28AA
5.	Mandatory Penalty for non levy or short levy of duties	11 AC	114A
6.	Refund of Export duty Refund of import duty – special cases	—	26 26A
7.	Claim for refund of duty	11B	27
8.	Interest on delayed refunds	11BB	27A
9.	Power not to recover duties not levied or short levied as a result of court decision. Wrong practice etc.	11C	28A
10.	Duties collected from buyer to be deposited with the department	11D	28B
11.	Interest on the amounts collected in excess of duty	11DD	
12.	Provisional attachment of property	11DD A	28 BA
13.	Consumer Welfare Fund	12C	
14.	Utilisation of Fund	12D	
15.	Interest on predeposit	35FF	129EE
16.	Amount of duty to be shown clearly in the bill/ invoice etc.	12A	28C
17.	Presumption that incidence of duty has been passed on to the buyer	12B	28D
18.	Power to grant exemption by Central Govt.	5A	25

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What are the various circumstances under which an assessee is entitled to claim refund of duties of Central Excise ?
 2. Explain the concept of 'relevant date' for computing time limit under Section 11B of the Central Excise Act, 1944.
 3. What is 'doctrine of unjust enrichment' with reference to Central Excise and what is the position of law in this regard ?
 4. Who can claim refund of Excise duty and what procedure is required to be followed for the same ?
 5. Under what situations the department is authorised to demand payment of duties of Excise in cases other than normal assessment ?
 6. Is the Government also empowered to waive off the recovery of duty not paid ? State the rule and circumstances under which it is exercised.

SUGGESTED READINGS

- (1) Central Excise Manual — *R.K. Jains, Centax Publications*
 - (2) Excise Law Times — *Centax Publications*
 - (3) Indirect Taxes—Law and Practice — *V.S. Datey*

CENTRAL EXCISE LAW

PART VIII: SMALL SCALE UNITS - APPLICABLE LAWS FOR EXCISE DUTY CONCESSIONS

After completion of this part student will

- Be well acquaint with the exemption available to small scale industries
- Be familiar with the conditions to be followed for claiming such exemption
- Be able to compute the total turnover for claiming exemption
- Be aware about the benefits or drawbacks of SSI exemption scheme

INTRODUCTION

Small-scale industries enjoy a privileged position in the whole industrial scenario of the country. Fiscal concessions are a part of the totality of the scheme of concessions to stimulate growth of small-scale sector. Both direct and indirect tax laws confer benefits on the small-scale sector. As regards Central Excise, a number of duty concessions exist for manufacturing activity without the aid of power, or for manufacturing activity upto a particular level - quantity of clearances, method and process of manufacture etc. These concessions are normally given in the form of exemptions by issuing necessary 'Exemption Notifications' under the relevant Central Excise Laws.

SALIENT FEATURES AND COVERAGE OF EXEMPTION NOTIFICATIONS

The general scheme of small-scale exemption which enables units to pay concessional rate of duty initially notified vide Notification No. 175/86—C.E. and modified vide Notification No. 1/93—C.E., has undergone further changes. Notification No. 1/93 was initially replaced by Notification No. 7/97—C.E. dated 1.3.1997 (as part of 1997 Budget Notifications) which was to come into force w.e.f. 1.4.1997. However, Notification No. 7/97—C.E. was superseded by another Notification No. 16/97—C.E. w.e.f. 1.4.1997 even before it could come into operation because of resistance from the SSI units as being harsh. Since Notification No. 16/97—C.E. did not allow MODVAT credit at all upto ₹100 lakhs clearances, besides other problems, a fresh Notification No. 38/97 was issued w.e.f. 27.6.1997 which provided MODVAT credit and gave option of availing benefit under any of the two Notifications, namely, 16/97—C.E. and 38/97—C.E., subject to certain conditions. These two notifications were then superseded by Notifications 8/98-C.E. and 9/98-C.E. both dated 2.6.1998 respectively. Notification 8/98-CE which superseded Notification No. 16/97-CE catered to SSI Units not availing MODVAT Credit and Notification 9/98-CE which superseded Notification 38/97-CE catered to those SSI units which decided to avail MODVAT Credit.

Till 31.03.2005, two *Notifications 8/2003 and 9/2003 dated 1.03.2003* were relevant for the exemption for Small Scale units. However, w.e.f. 1.04.2005, *Notification No. 9/2003 dated 1.03.2003* which provided concessional rate of duty of 60% of the normal rate with Cenvat credit has been rescinded vide *Notification No. 11/2005 C.E., dated 1.03.2005*. Further, *Notification No. 8/2003* has been amended to increase the eligibility limit for general SSI exemption from ₹300 lakh to ₹400 lakh. The manufacturer availing the notification has to satisfy certain conditions for availing the benefit and the goods manufactured should be covered under this notification. This is a beneficial notification where all entrepreneurs irrespective of their investment are eligible to avail the benefit.

GENERAL EXEMPTION SCHEME UNDER NOTIFICATION NO. 8/2003-C.E.

Small scale industries (SSIs) have an important place in Indian economy. They need special protection as

well as favourable treatment. The reasons are many like, they generate more employment, they help in regional development and balanced economic growth, more national income and more export earning, and so on.

Concessions under excise have other reasons also. The prices of the goods produced by the SSIs should be competitive and given the level of activity, they deserve some tax concessions. Even the cost benefit analysis is in favour of the SSIs. The cost of collection for SSIs is around 5% whereas it is below 1% for large industries. Hence, government is keen to offer some benefits by way of issuing notifications.

The provisions for exemption of Small Scale Industries are not contained in any section or rule of Central Excise Law. The provisions are contained in Notification No.8/2003 as amended from time to time.

SSIs – NOTIFICATION 8/2003-CE

In exercise of powers given by section 5A the Central Government has exempted the clearance for home consumption of excisable goods specified in the annexure to this notification from basic and special excise duty.

Small scale industry has no where been defined in excise laws. The benefits availed by units based on value of clearances are a clue to it. Those units manufacturing eligible goods specified in the notifications, and also qualifying the test of annual turnover are considered as small scale industries. In order to get the beneficial treatment under the Notification 8/2003-CE, the qualifying tests are: manufacture of eligible goods and their previous financial year's turnover being not more than Rs. 4 crore.[400 lakh]

VALUE OF CLEARANCES UP TO WHICH EXEMPTION IS AVAILABLE

As per this notification, the value of the clearance mentioned below shall be exempted from whole of the basic duty and special duty of excise:

S. No	Value of clearances	Rate of duty
1.	First clearances up to an aggregate value not exceeding one hundred and fifty lakh rupees made on or after the 1st day of April in any financial year.	Nil
2.	All clearances of the specified goods which are used as inputs for further manufacture of any specified goods within the factory of production of the specified goods.	Nil

Eligibility Criteria

1. Goods
2. Turnover of previous year

1. Goods must be specified goods which are other than those in the negative list given in the notification No. 8/2003 amended from time to time. Tobacco products, automobiles, explosives, primary iron and steel, ceramics, stainless steel pattas and patties, aluminium circles etc. are in the negative list.

Units manufacturing the above are not eligible for SSI exemption.

The honourable Supreme Court in **CCE v Khanna Industries 2007 S.C.** held that SSI exemption is **goods specific**.

2. Turnover: Under this notification, any unit whose value of goods cleared in the previous financial year was less than ₹4 crores are eligible for this exemption.

VALUE OF CLEARANCES TO BE EXCLUDED FOR CALCULATION OF LIMIT OF ₹150 LAKHS

For the purposes of determining the first clearances upto an aggregate value not exceeding 150 lakh rupees made on or after the 1st day of April in any financial year, the following clearances shall not be taken into account:-

- (a) clearances, which are exempt from the whole of the excise duty leviable thereon (other than an exemption based on quantity or value of clearances) under any other notification or on which no excise duty is payable for any other reason;
- (b) clearances bearing the brand name or trade name of another person, which are ineligible for the grant of this exemption. This is however, subject to exceptions
- (c) clearances of the specified goods which are used as inputs for further manufacture of any specified goods within the factory of production of the specified goods.
- (d) Clearances meant for export.

In *Bonanzo Engg. & Chemicals (P) Ltd*, 2012 (277) ELT 145 (S.C) , the Supreme Court held that the goods exempt under other notifications need not be included in the value of goods considered for exemption limit of Rs. 150 lakhs even if the assessee had paid duty thereon by mistake.

VALUE OF CLEARANCES TO BE EXCLUDED FOR CALCULATION OF LIMIT OF ₹400 LAKHS

For the purposes of determining the aggregate value of clearances exceeding Rs. 400 lakhs of all excisable goods for home consumption, the following clearances shall not be taken into account:

- (a) clearances of excisable goods without payment of duty-
 - (i) to a unit in a free trade zone; or
 - (ii) to a unit in a special economic zone; or
 - (iii) to a 100% export-oriented undertaking; or
 - (iv) to a unit in an Electronic Hardware Technology Park or Software Technology Park; or
 - (v) for their official use or supplied to projects funded by them, on which exemption of duty is available under Notification No.108/95- C.E. dated 28.08.1995.
- (b) clearances bearing the brand name or trade name of another person, which are ineligible for the grant of this exemption.
- (c) clearances of the specified goods which are used as inputs for further manufacture of any specified goods within the factory of production of the specified goods.
- (d) Clearances which are exempt from the whole of the excise duty leviable thereon under specific job work notifications, viz. Notification No. 214/86-C.E., dated 25.03.1986 or No. 83/94-C.E., dated 11.04.1994 or No. 84/94-C.E., dated 11.04.1994.

In short, the following table shows the turnover which is excluded for the purpose of calculating ₹4 crore in the previous financial year.

NO.	ITEMS
1.	Export turnover direct and through merchant exporter including supplies to SEZ units. [Except export to Bhutan]
2.	Deemed exports – Sale to EOU, EHTP/STP, UNO, International Agencies etc.
3.	Goods of others brand (subject to exceptions)
4.	Manufacture of intermediate product captively consumed unless the final product is generally exempt
5.	Job work amounting to manufacture
6.	Nil rated goods
7.	Inputs removed as such without processing

Illustration: Find out turnover from the following clearances made in the previous financial year.

	₹
Local sale	2.6 crore
Export to Bhutan	1.2 crore
Sale to an E.O.U	1.75 lac
Intermediate products manufactured as job worker and availed exemption Notification No. 214/86	23,000
Sale of inputs after partial process not amounting to manufacture.	34,000
Exports to China	44 lac
Sale to UNO Agencies under exemption notification	1.7 lac
Clearance of nil rated goods	2.8 crore
Goods of others brand cleared (50% of them were manufactured in a rural area)	0.2 crore

Solution:

₹ in crores

Local clearances as per SSI notification:

1. local sale	2.6
2. Export to Bhutan	1.2
3. 50% of branded goods manufactured in rural area	<u>0.1</u>
	<u>3.9</u>

- Notes:** (1) Export to Nepal in any currency is not a local clearance. It is to be considered as export turnover.
 (2) When goods of others brand are manufactured in rural area they are eligible for SSI exemption and hence includable in turnover

IMPORTANT NOTE: Turnover of exempted goods is included for calculating ₹ 400 lac but same is not includable for calculating ₹ 150 lac for the current year.

Points for consideration

1. Clubbing of Turnover:

The following turnovers are clubbed together to calculate the turnover achieved:

- by a manufacturer from all of his factories
- by different manufacturers in the same factory, during different shifts by different manufacturers in the same factory, during different parts of a year.

Illustration: A Ltd. is a company manufacturing plastic goods. it has two factories one at Jaipur and another at Noida. Following information in respect of the Two factories is available for the financial year 2012-2013

No.	Particulars	Jaipur factory ₹ In lacs	Noida factory ₹ In lacs
(i)	Goods cleared with own brand	75	100
(ii)	Clearances of plastic containers bearing brand name of Jolly Jams (to pack jam by them)	45	70
(iii)	Goods cleared to 100% EOU against form CT-3	90	80
(iv)	Export to Bhutan	50	60
(iv)	Job work under notification No. 214/ 86	65	55
(v)	Job work under notification No.84/ 94	85	95

Ascertain whether A Ltd. can avail exemption of small scale industry in the financial year 2013-2014.

Solution: The turnover of A Ltd. is to be clubbed. Item No. (ii) is eligible turnover as it falls under exceptions. Turnover of goods manufactured as a job worker availing exemption under the above two notifications is not to be added .

Total combined turnover of the two units in 2012-13 comes to ₹400 lacs. Hence the A Ltd. is eligible and it can avail exemption upto ₹150 lac turnover in the Financial year 2013-2014.

2. Valuation for the purpose of turnover is calculated on ad valorem basis either under Section 4 or Section 4A or 3(2) of the Central Excise Act, 1944. Assessable value of the goods removed in the immediate previous financial year shall be considered for determining the turnover.

3. Export to Bhutan is not considered as exports. It is taken as clearance for home consumption. Thus, export turnover of Bhutan shall be included for determining the limit of ₹150 lakh as well as ₹400 lakh.

CONDITIONS FOR CLAIMING THE EXEMPTIONS BASED ON CLEARANCES

The exemption based on value of clearances shall apply subject to the following conditions:

1. Option given to avail the exemption

(i) A manufacturer has the option not to avail the exemption contained in this notification and instead pay the normal rate of duty on the goods cleared by him. Such option shall be exercised before effecting his first clearances at the normal rate of duty. Such option shall not be withdrawn during the remaining part of the financial year;

(ii) If option is exercised, the manufacturer shall inform in writing to the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise with a copy to the Superintendent of Central Excise giving the following particulars, namely:-

- (a) name and address of the manufacturer;
- (b) location/locations of factory/factories;
- (c) description of inputs used in manufacture of specified goods ;
- (d) description of specified goods produced;
- (e) date from which option under this notification has been exercised;
- (f) aggregate value of clearances of specified goods (excluding the value of clearances referred to in paragraph 3 of this notification) till the date of exercising the option;

2. Cenvat credit shall not be available on inputs

The manufacturer shall not avail the credit of duty on inputs under rule 3 or rule 11 of the CENVAT Credit Rules, 2004 (herein after referred to as the said rules), paid on inputs used in the manufacture of the specified goods cleared for home consumption, the aggregate value of first clearances of which does not exceed rupees one hundred fifty lakhs;

The Cenvat credit shall be available for inputs used in the manufacture of specified goods bearing the brand name or trade name of another person.

3. Cenvat credit shall not be available on capital goods

The manufacturer also does not utilise the credit of duty on capital goods under rule 3 or rule 11 of the said rules, paid on capital goods, for payment of duty, if any, on the aforesaid clearances, the aggregate value of first clearances of which does not exceed rupees one hundred fifty lakhs.

BENEFITS TO SSIs

No registration with the Directorate of Industry is necessary for availing of the exemption under SSI Scheme. Also, no registration is required, if turnover is less than Rs. 150 lakhs and the goods are exempted. Only a declaration is required if turnover crosses 90 lakhs.

SSIs have to file return once in a quarter, i.e. by 10th of the following quarter and can make the payment of duty quarterly by 5th of the month in the next quarter or 6th where electronic payment is made. Excise officers can visit the premises of SSIs only with the specific permission of the Assistant Commissioner.

GOODS BEARING THE BRAND NAME OF OTHERS EXCEPTIONS

The benefit of Exemption notification is not available to goods manufactured under others brand name. It is

immaterial whether the brand name is registered or not. However, the exemption is still available in the following cases:

- (i) Components or parts of machinery, equipment or appliances cleared for use as **original equipment** in the manufacture of the said machinery, equipment appliance.
 - (ii) The exemption is available for the goods bearing a brand name of-
 - The State Khadi and Village Industry Board [SKVIB]
 - Khadi and Village Industries Commission; [KVIC]
 - The National Small Industries Corporation [NSIC]
 - A State Small Industries Development Corporation; [SSIDC] or
 - A State Small Industries Corporation [SSIC]
1. Where the specified (eligible) goods are manufactured in a factory located in a rural area, they are eligible even if they are bearing the brand name of others.
 2. account books, registers, writing pads and file folders under chapter 48 of CETA.
 3. where the specified goods are in the nature of packing material such as paper board, metal containers ,adhesive tapes including **plastic bottles, plastic containers and printed laminated rolls.**

“Packing material includes labels of all kinds.”

Explanation: For the purposes of this notification,-

- (A) "brand name" or "trade name" means a brand name or a trade name, whether registered or not, that is to say, a name or a mark, such as symbol, monogram, label, signature or invented word or writing which is used in relation to such specified goods for the purpose of indicating, or so as to indicate a connection in the course of trade between such specified goods and some person using such name or mark with or without any indication of the identity of that person;
- (B) where the specified goods manufactured by a manufacturer bear a brand name or trade name, whether registered or not, of another manufacturer or trader, such specified goods shall not, merely by reason of that fact, be deemed to have been manufactured by such other manufacturer or trader;

CENVAT CREDIT IMPLICATIONS AND APPLICABLE PROVISIONS

- The SSI unit after crossing the turnover limit of Rs. 1.5 crore, can start availing and utilizing cenvat credit .
- Before reaching the turnover of 1.5 crore it can avail cenvat credit on capital goods as per Rule 6(4) of Cenvat Credit Rules, but cannot utilize the same under the notification. It means it can start utilizing the credit on capital goods only when its turnover goes beyond Rs.1.5 crore.
- When the eligible SSI unit wants to go back to exemption scheme, it can do only in the beginning of the financial year. As per rule 11(2) of Cenvat Credit Rules , at the time of switch over, it has to pay the amount of duty attributable to the inventory lying as stock by debiting the cenvat credit account or otherwise Any balance remaining after writing off, will lapse and it cannot be utilized for any purpose whatsoever.

Illustration

A unit manufacturing goods eligible for exemption under SSI Scheme has given the following information:

Turnover during 2011-12: ₹ 8.7 crore.

Which included the following:

Export to China	₹ 3.2 crore
Export to Bhutan	₹ 1.8 crore
Sale to an SEZ unit	₹ 1 crore
Sale of nil rated goods in India	₹ 70 lakh

Turnover during 2012-13 ₹ 2 crore

Total duty paid on inputs used for achieving the above turnover of ₹ 2 crore is 20 lakh rupees.

Duty payable on output is 16%.

Find out:

- (i) Whether the unit is eligible to enjoy SSI benefit under Notification No. 8/2003-CE. If so, what is the duty payable in the Year 2012-13.
- (ii) What would be duty liability of the assessee if he does not avail SSI exemption?
- (iii) Which course of action will be beneficial to the assessee?

Solution:

(i) If the turnover in the previous financial year is below ₹4 crore, the unit is eligible for exemption in the current Financial Year.

Turnover of the previous year 2011-12 will be calculated as follows:

	₹
Total turnover	8,70,00,000
Less : Export turnover to China	3,20,00,000
Sale to SEZ unit	1,00,00,000
Sale of nil rated goods	<u>70,00,000</u> <u>4,90,00,000</u>
	<u>3,80,00,000</u>

Since the turnover is below ₹ 4 crore, the unit is eligible for SSI Benefit.

In the year 2012- 13, duty liability is as follows:

	₹
Total turnover	2.0 crore
Less: Exemption turnover	<u>1.5 crore</u>
Dutiable turnover	<u>0.5 crore</u>
Duty @16% on one crore is Rs. 16/100 x 50,00,000 i.e. Rs. 8,00,000	
Add: Education cess @ 2% i.e.	16,000
Add: SHEC @1%	<u>8,000</u>
Total duty payable	8,24,000
Less: CENVAT Credit available i.e. 25% of 20 lakh	<u>5,00,000</u>
Net duty payable	₹ <u>3,24,000</u>

Note: 25% of total inputs is eligible for credit as the input credit cannot be taken on the exempted turnover.

(ii) Total duty liability if SSI benefit is not availed:

Total turnover	₹ 2,00,00,000
Duty payable including education cess & SHEC (i.e. 16.32% of 2 crore)	32,96,000
Duty payable is	₹ 32,96,000
Less: CENVAT Credit available	20,00,000
Net duty payable	12,96,000

(iii) Since the net duty payable under normal scheme is ₹12,96,000 as against ₹ 3,24,000 under SSI Scheme, the assessee is advised to avail the exemption under Notification No. 8/2003-CE.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What are the excise duty concessions to the small scale sector?
2. What is the General Small Scale Exemptions Scheme ? In respect of what excisable goods this exemption apply ?
3. Who can avail of the exemption under the general small scale exemption scheme?
4. If a factory is being run during any financial year by different persons, how will the eligibility be determined?
5. In determining the value of clearances, will the value of clearances of goods which are wholly exempted from duty or chargeable to nil duty be included?
6. What are the concessions available to a small scale unit under the General Exemption Scheme ? What is the limit up to which excise duty is fully exempted under the currently applicable notifications ?
7. An SSI unit had a turnover of ₹350 lakhs in the previous financial year.
 - It has effected the following clearances in the current year:
 - Sale to exporter on form H under CST Act ₹75 lakh.
 - Exports to Myanmar (Burma) ₹ 1.12 crore.
 - Exempted goods ₹54 lakhs.
 - account books, registers, writing pads bearing the brand name of others Rs 25 lakhs.
 - Goods manufactured in a rural area but exported to Bhutan Rs. 35 lakhs.
 - Sale of inputs as such ₹ 30 lakh
 - Local sale ₹ 34 lakhs.
 - The unit claims that its turnover is below 1.5 crore and hence not liable to pay any duty. Comment.
8. Is there any exemption for goods manufactured or cleared on/for job work basis by an SSI unit?

SUGGESTED READINGS

- (1) Central Excise Guide for Small Scale Industry — *G. Sarangi, Centax Publications, New Delhi*
- (2) Excise Law Times — *Centax Publications, New Delhi*
- (3) Central Excise Tariff — *R. K. Jain, Centax Publications, New Delhi*
- (4) Central Excise Law Manual — *R. K. Jain, Centax Publications, New Delhi.*

CENTRAL EXCISE LAW

PART IX: OFFENCES, SEARCH & SEIZURE AND ADJUDICATION PROCEDURES

This part covers the following provisions:

- Offences and penalties
- Search, seizure and confiscation provisions
- Adjudication Procedure

After completion of this part, student will have the understanding of

- Which acts are considered as offence and what are the penal provisions against these offences under the central excise law
- When the process of search and seizure can be initiated
- What are the confiscation provisions
- Powers of Adjudication of confiscation and Penalties.

OFFENCES AND PENALTIES (SECTION 9)

Section 9(1) of the Central Excise Act provides for penalties if the following offences are committed:

- (a) (i) Possession of goods specified in the second schedule for which restrictions are prescribed in accordance with the provisions of section 8 or
 - (ii) Transit any prohibited excisable goods prescribed under the rules made under section 37(2)(iii) from any part of India to any other part or
 - (iii) The person not get himself registered under section of the Act as specified under the rules made under clause (xxvii) of sub-section (2) of section 37;
- (b) evades the payment of any duty payable under this Act;
- (c) removes any excisable goods in contravention of any of the provisions of this Act or any rules made thereunder or in any way concerns himself with such removal;
- (d) acquires possession of, or in any way concerns himself in transporting, depositing, keeping, concealing, selling or purchasing, or in any other manner deals with any excisable goods which he knows or has reason to believe are liable to confiscation under this Act or any rule made thereunder;
- (e) contravenes any of the provisions of this Act or the rules made thereunder in relation to credit of any duty allowed to be utilised towards payment of excise duty on final products;
- (f) fails to supply any information which he is required by rules made under this Act to supply or (unless with a reasonable belief, the burden of proving which shall be upon him, that the information supplied by him is true) supplies false information;
- (g) attempts to commit, or abets the commission of, any of the offences mentioned in clauses (a) and (b) of this section;

The above offences shall be punishable,-

- (i) in the case of an offence relating to any excisable goods, the duty leviable thereon under this Act

exceeds fifty lakh of rupees, with imprisonment for a term which may extend to seven years and with fine:

However, in the absence of special and adequate reasons to the contrary to be recorded in the judgment of the Court such imprisonment shall not be for a term of less than six months;

- (ii) in any other case, with imprisonment for a term which may extend to three years or with fine or with both.

If any person convicted of an offence under this section is again convicted of an offence under this section, then, he shall be punishable for the second and for every subsequent offence with imprisonment for a term which may extend to seven years and with fine:

However, in the absence of special and adequate reasons to the contrary to be recorded in the judgment of the Court such imprisonment shall not be for a term of less than six months.

The following shall not be considered as special and adequate reasons for awarding a sentence of imprisonment for a term of less than six months, namely:-

- (i) the fact that the accused has been convicted for the first time for an offence under this Act;
- (ii) the fact that in any proceeding under this Act, other than a prosecution, the accused has been ordered to pay a penalty or the goods in relation to such proceedings have been ordered to be confiscated or any other action has been taken against him for the same act which constitutes the offence;
- (iii) the fact that the accused was not the principal offender and was acting merely as a carrier of goods or otherwise was a secondary party in the commission of the offence;
- (iv) the age of the accused.

CERTAIN OFFENCES TO BE NON-COGNIZABLE (SECTION 9A)

Notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), offences under section 9, except the offences referred to in Section 9A(1A), relating to excisable goods where the duty leviable thereon under this Act exceeds fifty lakh rupees and payment of duty evaded or any of the provisions of this act or the rules made there under in relation to credit of any duty allowed to be utilized towards payment of excise duty of final products contravened, shall be non-cognizable within the meaning of that Code and therefore such offences referred in Section 9A(1A) are cognizable and non-bailable. [(Section 9A(1) & (1A)].

Any offence under this Chapter may, either before or after the institution of prosecution, be compounded by the Chief Commissioner of Central Excise on payment, by the person accused of the offence to the Central Government, of such compounding amount and in such manner of compounding as may be prescribed [Section 9(2)].

However, the following offences are not compoundable;

- (a) a person who has been allowed to compound once in respect of any of the following offences;
 - (1) Possession of goods specified in the second schedule for which restrictions are prescribed in accordance with the provisions of section 8 or
 - (2) Transit any prohibited excisable goods prescribed under the rules made under section 37(2)(iii) from any part of India to any other part or

- (3) The person not get himself registered under section of the Act as specified under the rules made under clause (xxvii) of sub-section (2) of section 37;
 - (4) evades the payment of any duty payable under this Act;
 - (5) removes any excisable goods in contravention of any of the provisions of this Act or any rules made thereunder or in any way concerns himself with such removal;
 - (6) acquires possession of, or in any way concerns himself in transporting, depositing, keeping, concealing, selling or purchasing, or in any other manner deals with any excisable goods which he knows or has reason to believe are liable to confiscation under this Act or any rule made thereunder;
 - (7) contravenes any of the provisions of this Act or the rules made thereunder in relation to credit of any duty allowed to be utilised towards payment of excise duty on final products;
 - (8) fails to supply any information which he is required by rules made under this Act to supply or (unless with a reasonable belief, the burden of proving which shall be upon him, that the information supplied by him is true) supplies false information;
- (b) a person who has been accused of committing an offence under this Act which is also an offence under the Narcotic Drugs and Psychotropic Substances Act, 1985 (61 of 1985);
 - (c) a person who has been allowed to compound once in respect of any offence under this Chapter for goods of value exceeding rupees one crore;
 - (d) a person who has been convicted by the court under this Act on or after the 30th day of December, 2005.

OFFENCES BY COMPANIES (SECTION 9AA)

Where an offence under this Act has been committed by a company, every person who, at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly [Section 9AA(1)].

However, nothing contained in this sub-section shall render any such person liable to any punishment provided in this Act, if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence [Proviso to section 9AA(1)].

Notwithstanding anything contained in sub-section (1), where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly [Section 9AA(2)].

- (a) "company" means any body corporate and includes a firm or other association of individuals; and
- (b) "director" in relation to a firm means a partner in the firm.

POWER OF COURT TO PUBLISH NAME, PLACE OF BUSINESS, ETC., OF PERSONS CONVICTED UNDER THE ACT (SECTION 9B)

Where any person is convicted under this Act for contravention of any of the provisions thereof, it shall be competent for the Court convicting the person to cause the name and place of business or residence of such

person, nature of the contravention, the fact that the person has been so convicted and such other particulars as the Court may consider to be appropriate in the circumstances of the case, to be published at the expense of such person, in such newspapers or in such manner as the Court may direct [Section 9B(1)].

No publication shall be made until the period for preferring an appeal against the orders of the Court has expired without any appeal having been preferred, or such an appeal, having been preferred, has been disposed of [Section 9B(2)].

As per section 9B(3), the expenses of any publication shall be recoverable from the convicted person as if it were a fine imposed by the Court.

PRESUMPTION OF CULPABLE MENTAL STATE (SECTION 9C)

As per section 9C(1) In any prosecution for an offence under this Act which requires a culpable mental state on the part of the accused, the Court shall presume the existence of such mental state but it shall be a defence for the accused to prove the fact that he had no such mental state with respect to the act charged as an offence in that prosecution.

"culpable mental state" includes intention, motive, knowledge of a fact, and belief in, or reason to believe, a fact.

II. SEARCH AND SIEZURE

Under Central Excise Act, certain powers are given to the Excise Officers and which are very essential in that the departmental officials would like to have close surveillance and vigilance over the assessee as to what he is doing at the factory wherein any excisable goods are manufactured; whether the assessee maintains proper records, whether the assessee follows prescribed procedures etc., all in an attempt to safeguard the interests of revenue. These powers assume all the more importance in view of the fact that now the self-removal procedure (SRP) stands extended to all the excisable goods. SRP is a manifestation of the Department's faith in the assessee and the assessee has the freedom to remove the goods without the requirement of the presence of an excise official at the time of each clearance of the excisable goods from the factory. Naturally, when the assessee is being trusted to that extent, the Departmental officers should also have powers to enter the premises with a view of finding out whether the benefit given to the assessee is being in any manner put to misuse or the assessee is indulging in any other practices with a result the duty due to the Department is being evaded.

Let's discuss the powers of search and seizure with Central Excise Officers;

(A) POWER OF SEARCH AND SEIZURE (SECTION 12F)

Where the Joint commissioner of Central Excise or Additional Commissioner of Central Excise or such other Central Excise Officer as may be notified by the Board has reasons to believe that any goods liable to confiscation or any documents or books or things which in his opinion shall be useful for or relevant to any proceedings under this Act, are secreted in any place, he may authorise in writing any Central Excise Officer to search and seize or may himself search and seize such documents or books or things.

The provisions of the Code of Criminal Procedure, 1973 relating to search and seizure shall, so far as may be, apply to search and seizure under this section subject to the modification that subsection (5) of section 165 of the said Code shall have effect as if for the word "Magistrate", wherever it occurs, the words "Commissioner of Central Excise" were substituted.

(B) POWER TO ARREST (SECTION 13)

(1) If an officer of Central Excise empowered in this behalf by general or special order of the Commissioner

of Central Excise has reason to believe that any person has committed an offence punishable under this Act, he may arrest such person and shall, as soon as may be, inform him of the grounds for such arrest.

(2) Every person arrested under sub-section (1) for an offence shall, without unnecessary delay, be taken to a Magistrate.

(3) Where an officer of Central Excise has arrested any person under subsection (1), for any offence (other than an offence punishable for a term of imprisonment of three years or more under section 9), he shall, for the purpose of releasing such person on bail or otherwise, have the same powers and be subject to the same provisions as the officer-in-charge of a police station has, and is subject to, under the Code of Criminal Procedure, 1973.

(4) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, all offences under this Act (except an offence punishable for a term of imprisonment of three years or more under section 9) shall be liable.

(5) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, all offences punishable for a term of imprisonment of three years or more under section 9 shall be cognizable.

(C) BAIL FOR OFFENCE PUNISHABLE FOR A TERM OF IMPRISONMENT OF THREE YEARS OR MORE UNDER SECTION 9 NOT TO BE GRANTED WITHOUT HEARING PUBLIC PROSECUTOR (SECTION 13A)

(1) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, no person Accused of an offence punishable for a term of imprisonment of three years or more under section 9 shall be released on bail or on his own bond unless—

- (i) the public prosecutor has been given an opportunity to oppose the application for such release; and
- (ii) where the public prosecutor opposes the application, the Magistrate is satisfied that there are reasonable grounds for believing that he is not guilty of such offence and that he is not likely to commit any offence while on bail:

However, a person who is under the age of eighteen years or is a woman or is sick or infirm, may be released on bail if the Magistrate so directs.

(2) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, no police officer shall, save as otherwise provided under this Act, investigate into an offence under this Act unless specifically authorised by the Central Government by a general or special order, and subject to such conditions as may be specified in the order.

(D) SEARCHES AND ARRESTS HOW TO BE MADE (SECTION 18)

All searches under this Act or the rules made thereunder and all arrests under this Act shall, save as otherwise provided under this Act, be carried out in accordance with the provisions of the Code of Criminal Procedure, 1973(2 of 1974), relating respectively to searches and arrests under that Code.

PROCEDURE TO BE FOLLOWED BY OFFICER-IN-CHARGE OF POLICE STATION (SECTION 20)

The officer-in-charge of a police station to whom any person is forwarded shall, where the offence is non-cognizable, either admit him] to bail to appear before the Magistrate having jurisdiction, or in default of bail forward him in custody to such Magistrate in accordance with the provisions of this Act.

(E) VEXATIOUS SEARCH, SEIZURE, ETC., BY CENTRAL EXCISE OFFICER (SECTION 22)

Any Central Excise or other Officer exercising powers under this Act or under the rules made thereunder who-

- (a) without reasonable ground of suspicion searches or causes to be searched any house, boat or place;
- (b) Vexatious and unnecessarily detains, searches or arrests any person;
- (c) vexatiously and unnecessarily seizes the movable property of any person, on pretence of seizing or searching for any article liable to confiscation under this Act;
- (d) commits, as such officer, any other act to the injury of any person, without having reason to believe that such act is required for the execution of his duty;

shall, for every such offence, be punishable, with fine which may extend to two thousand rupees.

Any person wilfully and maliciously giving false information and so causing an arrest or, a search to be made under this Act shall be punishable with fine which may extend to two thousand rupees or with imprisonment for a term which may extend to two years or with both.

FAILURE OF CENTRAL EXCISE OFFICER IN DUTY (SECTION 23)

If the Central Excise Officer ceases or withdraws, or refuses to perform the duty of his office without the permission of the central excise officer or without giving his intentions in writing by way of notice then, he shall be punishable with imprisonment for a term of 2 months which may extend to three months, or with fine which may extend to three months or with both.

RULES FOR SEARCH AND SEIZURE

Central Excise Rules, 2002 deals with various matters relating to access to registered premises, power to stop, search etc. by authorised officials of the Central Excise Department.

Rules 22 to 30 of the Central Excise Rules, 2002 deal with entire gamut of access, search, seizure, confiscation and penalty. These rules are self-explanatory. They are reproduced hereinbelow:

ACCESS TO A REGISTERED PREMISES (RULE 22)

(1) An officer empowered by the Commissioner in this behalf shall have access to any premises registered under these rules for the purpose of carrying out any scrutiny, verification and checks as may be necessary to safeguard the interest of revenue.

(2) Every assessee, and first stage and second stage dealer shall furnish to the officer empowered under sub-rule (1), a list in duplicate, of-

- (i) all the records prepared and maintained for accounting of transaction in regard to receipt, purchase, manufacture, storage, sales or delivery of the goods including inputs and capital goods, as the case may be;
- (ii) all the records prepared and maintained for accounting of transaction in regard to payment for input services and their receipt or procurement; and
- (iii) all the financial records and statements including trial balance or its equivalent.

(3) Every assessee, and first stage and second stage dealer shall, on demand make available to the officer empowered under sub-rule (1) or the audit party deputed by the Commissioner or the Comptroller and

Auditor- General of India, or a cost accountant or chartered accountant nominated under section 14A or section 14AA of the Act,-

- (i) the records maintained or prepared by him in terms of sub-rule (2);
- (ii) the cost audit reports, if any, under section 233B of the Companies Act, 1956(1 of 1956); and
- (iii) the income-tax audit report, if any, under section 44AB of the Income-tax Act, 1961 (43 of 1961), for the scrutiny of the officer or the audit party or the cost accountant or chartered accountant, within the time limit specified by the said officer or the audit party or the cost accountant or chartered accountant, as the case may be.

POWER TO STOP AND SEARCH (RULE 23)

Any Central Excise Officer, may search any conveyance carrying excisable goods in respect of which he has reason to believe that the goods are being carried with the intention of evading duty.

POWER TO DETAIN OR SEIZE GOODS (RULE 24)

If a Central Excise Officer, has reason to believe that any goods, which are liable to excise duty but no duty has been paid thereon or the said goods were removed with the intention of evading the duty payable thereon, the Central Excise Officer may detain or seize such goods.

RETURN OF RECORDS (RULE 24A)

The books of accounts or other documents, seized by the Central Excise Officer or produced by an assessee or an other person, which have not been relied on for the issue of notice under the Act or the rules made thereunder, shall be returned within thirty days of the issue of said notice or within 30 days from the date of expiry of the period for issue of said notice:

However, the commissioner of Central Excise may order for the retention of such books of accounts or documents for reasons to be recorded in writing and the Central Excise Officer shall intimate to the assessee or such person about such retention.

CONFISCATION AND PENALTY (RULE 25)

Subject to the provisions of Section 11AC of the Act, if any producer, manufacturer, registered person of a warehouse or a registered dealer:

- (a) removes any excisable goods in contravention of any of the provisions of these rules or the notifications issued under these rules; or
 - (b) does not account for any excisable goods produced or manufactured or stored by him; or
 - (c) engages in the manufacture, production or storage of any excisable goods without having applied for the registration certificate required under Section 6 of the Act; or
 - (d) contravenes any of the provisions of these rules or the notifications issued under these rules with intent to evade payment of duty, then, all such goods, shall be liable to confiscation and the producer or manufacturer or registered person of the warehouse or a registered dealer, as the case may be, shall be liable to a penalty not exceeding the duty on the excisable goods in respect of which any contravention of the nature referred to in clause (a) or clause (b) or clause (c) or clause (d) has been committed, or rupees two thousand, whichever is greater.
- (2) An order shall be issued by the Central Excise Officer, following the principles of natural justice.

PENALTY FOR CERTAIN OFFENCES (RULE 26)

Any person who acquires possession of, or is in any way concerned in transporting, removing, depositing, keeping, concealing, selling or purchasing or in any other manner deals with any excisable goods which he

knows or has reason to believe are liable to confiscation under the Act or these rules, shall be liable to a penalty not exceeding the duty on such goods or rupees two thousand, whichever is greater.

(2) Any person, who issues-

- (i) an excise duty invoice without delivery of the goods specified therein or abets in making such invoice; or
- (ii) any other document or abets in making such document, on the basis of which the user of said invoice or document is likely to take or has taken any ineligible benefit under the Act or the rules made thereunder like claiming of CENVAT credit under the CENVAT Credit Rules, 2004 or refund, shall be liable to a penalty not exceeding the amount of such benefit or five thousand rupees, whichever is greater

GENERAL PENALTY (RULE 27)

A breach of these rules shall, where no other penalty is provided herein or in the Act, be punishable with a penalty which may extend to five thousand rupees and with confiscation of the goods in respect of which the offence is committed.

ON CONFISCATION, PROPERTY TO VEST IN THE CENTRAL GOVERNMENT (RULE 28)

- (1) When any goods are confiscated under these rules, such thing shall thereupon vest in the Central Government.
- (2) The Central Excise Officer adjudging confiscation shall take and hold possession of the things confiscated, and every Officer of Police on the requisition of such Central Excise Officer, shall assist him in taking and holding such possession.

DISPOSAL OF GOODS CONFISCATED (RULE 29)

Goods of which confiscation has been adjudged and in respect of which the option of paying a fine in lieu of confiscation has not been exercised, shall be sold, destroyed or otherwise disposed of in such manner as the Commissioner may direct.

STORAGE CHARGES IN RESPECT OF GOODS CONFISCATED AND REDEEMED (RULE 30)

If the owner of the goods, the confiscation of which has been adjudged, exercises his option to pay fine in lieu of confiscation he may be required to pay such storage charges as may be determined by the adjudicating officer.

POWERS OF ADJUDICATION

Sections 33 to 34A of the Central Excise Act, 1944 deals with adjudication of confiscations and penalties. These sections provides for powers of adjudication to Officers of Central Excise where anything is liable to confiscation or any person is liable to penalty under the Act, along with giving them the option to pay fine in lieu of confiscation etc. These sections are reproduced below:

Where under this Act or by rules made thereunder anything is liable to confiscation or any person is liable to penalty, such confiscation or penalty may be adjusted:

- (a) without limit by a Commissioner of Central Excise;
- (b) upto confiscation of goods not exceeding five hundred rupees in value and imposition of penalty not exceeding two hundred and fifty rupees by an Assistant Commissioner of Central Excise.

Provided that the Central Board of Excise and Customs constituted under the Central Board of Revenues Act, 1963, may in the case of any officer performing the duties of an Assistant Commissioner of Central Excise, reduce the limits indicated in clause (b) of this section and may confer on any officer of the powers indicated in clause (a) of this section.

Section 33A has been inserted by the Finance (No. 2) Act, 2004 providing for adjudication procedure. As per this Section, an adjudicating authority provides an opportunity of being heard to a party in a proceeding, if the party so desires. Such authority may grant time, from time to time, to the parties or any of them and adjourn the hearing for reasons to be recorded in writing. However, no such adjournment shall be granted more than three times to a party during the proceeding.

OPTION TO PAY FINE IN LIEU OF CONFISCATION (SECTION 34)

Whenever confiscation is adjudged under this Act or the rules made thereunder, the Officer adjudging it, shall give the owner of the goods an option to pay fine in lieu of confiscation, such fine as the officer thinks fit.

CONFISCATION AND PENALTY NOT TO INTERFERE WITH OTHER PUNISHMENTS (SECTION 34A)

No confiscation made or penalty imposed under the provisions of the Act or of any rules made thereunder shall prevent infliction of any other punishment to which the person affected thereby is liable, under the provisions of this Act or under any other law.

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. Explain the provisions of vexatious seizure as given under section 22 of the Central Excise Act, 1944?"
 2. What are provisions of search and seizure under Central Excise.
 3. Discuss the powers of central excise officer to summon persons to give evidence and produce documents in inquiries under the Act.
 4. State provisions of Central Excise Act, 1944 in relation to arrest of a person. Who has the power to arrest and subject to what conditions?
 5. What do you mean by Adjudicating Authority? Who has the power of adjudication.

SUGGESTED READINGS

- (1) Central Excise Manual — *R.K. Jain, Centax Publications*
 - (2) Excise Law Times — *Centax Publications*

Lesson 6

Customs Law

LESSON OUTLINE

This lesson is divided into the following parts:

- I INTRODUCTION AND BASIC CONCEPTS OF CUSTOMS LAW
- II VALUATION, ASSESSMENT OF IMPORTED AND EXPORT GOODS AND PROCEDURAL ASPECTS
- III ARRIVAL OR DEPARTURE AND CLEARANCE OF IMPORTED OR EXPORT GOODS
- IV WAREHOUSING, DUTY DRAWBACK, BAGGAGE AND MISCELLANEOUS PROVISIONS
- V SEARCH, SEIZURE, CONFISCATION OF GOODS, OFFENCES AND PENALTIES

LEARNING OBJECTIVES

The Custom duty derived its value from the word “custom” under which whenever a merchant entered a Kingdom with his merchandise had to give some gift to the king. Subsequently, this custom formalized into the levy of custom duty or tax on goods imported into and exported from the country was organized through various laws during the British period. After Independence the Sea Customs Act 1878, the Land Customs Act, 1924 and other allied enactments were repealed by a consolidating and amending legislation entitled the Customs Act, 1962. Similarly the Indian Customs Act, 1934 was repealed by the Customs Tariff Act, 1975(CTA).

At the end of this lesson, the students will

- Have the understanding of the basic and practical aspects of customs law
- Be able to value the imported and export goods for payment of duty
- Understand clearance procedures involved in importation and exportation of goods
- Familiar with the warehousing, duty drawback and baggage provisions
- Have knowledge of search, seizure, penalty provisions thereto
- Be familiar with the adjudication provisions.

As per the Customs Act, 1962 the Central Board of Excise and Customs has given the powers to appoint Customs Ports, Airports and Inland Container Depots (ICD), where the imported goods can be brought in for unloading or export goods loaded. Similarly, powers have been given to the Board to notify places as Land Customs Stations (LCS) for clearance of goods imported or exported by land or by inland water.

CUSTOMS LAW

PART I: INTRODUCTION AND BASIC CONCEPTS OF CUSTOMS LAW

After going through this part you will be able to understand:

- Meaning and objects of customs duty
- Scope and coverage of custom law
- Types of custom duties
- Rate of custom duties applicable
- Definitions and concepts

INTRODUCTION

Custom Duty is imposed under the Customs Act formulated in 1962 mandated by the Constitution of India under the Article 265, which states that "no tax shall be levied or collected except by authority of law. Entry No. 83 of List I to Schedule VII of the Constitution empowers the Union Government to legislate and collect duties on import and exports. The Customs Act, 1962 is the basic statute which governs entry or exit of different categories of vessels, crafts, goods, passengers etc., into or outside the country. The Act extends to the whole of the India.

Customs Act, 1962 just like any other tax law is primarily for the levy and collection of duties but at the same time it has the other and equally important purposes such as:

- (i) regulation of imports and exports;
- (ii) protection of domestic industry;
- (iii) prevention of smuggling;
- (iv) conservation and augmentation of foreign exchange and so on.

Section 12 of the Custom Act provides that duties of customs shall be levied at such rates as may be specified under the Customs Tariff Act, 1975 on goods imported into or exported from India.

STATUTORY PROVISIONS OF CUSTOMS ACT, 1962

Customs Act, 1962 came into force from 1-2-1963, it extends to whole of India. The whole Act is divided into XVII chapters comprising of 161 sections.

Table showing the contents of Customs Act, 1962

Chapter No. and Title	Sections	Contents
I. Preliminary	Section 1 to 2	Short title, extent and commencement and Definitions
II. Officers of Customs	Section 3 to 6	Appointment and powers of officers of customs
III. Appointment of Customs Ports, Airports, Warehousing Stations etc.	Section 7 to 10	Appointments and powers of Customs Ports, Airports, Warehousing Stations etc.

IV.	Prohibitions on importation and exportation of goods	Section 11	Powers to prohibit import and export of goods
IVA.	Detection of illegally imported goods and prevention of the disposal thereof	Sections 11A to 11G	Provisions for illegal importation of notified goods and prevention of the disposal thereof
IVB.	Prevention or Detection of Illegal Export of Goods	Sections 11H to 11M	Provisions for illegal export of specified goods
IVC.	Power to exempt from the provisions of Chapters IVA and IVB	Section 11N	Power to exempt
V.	Levy of, and Exemption from, Customs Duties	Sections 12 to 28BA	Chargeable section, valuation of goods, Recovery and refund of duty
VA.	Indicating amount of duty in the price of goods, etc., for purpose of refund	Section 28C to 28D	Price of goods and incidence of duty passed on to the buyer
VB.	Advance Rulings	Section 28E to 28M	Provisions for advance ruling such as authority, application, procedure and powers of authority
VI.	Provisions relating to conveyances carrying imported or exported goods	Sections 29 to 43	Arrival or departure of goods, delivery of export manifest or export report
VII.	Clearance of imported goods and export goods	Sections 44 to 51	Clearance of import and export goods other than by way of baggage and postal articles.
VIII.	Goods in Transit	Sections 52 to 56	Transit and transshipment of goods
IX.	Warehousing	Section 57 to 73	Provision relating to public and private warehouse
X.	Drawback	Sections 74 to 76	Duty drawback on re-export of duty paid goods or material used in the manufacture of goods
XA.	Special Provisions relating to Special Economic Zone	Sections 76A to 76N	Omitted
XI.	Special provisions regarding baggage, goods imported or exported by post, and stores	Section 77 to 90	Special provisions regarding baggage, goods imported or exported by post, and stores
XII.	Provisions relating to coastal goods and	Section 91 to 99	Provisions relating to coastal goods and vessels carrying coastal goods other than

vessels carrying coastal goods		baggage and stores
XIII. Searches, seizure and arrest	Section 100 to 110A	Power to search, inspect, examine persons and seizure of goods, documents and things
XIV. Confiscation of goods and conveyances and imposition of penalties	Section 111 to 127	Adjudication proceedings and confiscation of goods.
XIVA. Settlement of cases	Sections 127A to 127N	Provisions relating to Settlement Commission
XV. Appeals and Revision	Sections 128 to 131C	Adjudication proceedings
XVI. Offences and Prosecutions	Section 132 to 140A	Offences and cognizance of offences
XVII. Miscellaneous	Section 141 to 161	Conveyances, duty deferment, license to Customs house agent, appearance by authorised representative, delegation of power etc.

LIMBS OF CUSTOMS LAW

Customs Act, 1962 and Customs Tariff Act, 1975 must be read with rules and regulations. The rule making power is delegated to the Central Government while the regulation making power delegated to the Central Board of Excise and Customs.

There are a number of rules and regulation prescribed from time to time to carry the objective of the Act. Some of the rules and regulations are enumerated here as follows:

- Baggage Rules ,1998
- Customs and Central Excise Duties and Service Tax Drawback Rules,1995
- Re-Export of Imported Goods (Drawback of Customs Duties) Rules, 1995
- Customs Valuation (Determination of Price of Imported Goods) Rules, 2007
- Customs Valuation (Determination of Value of Export Goods) Rules, 2007
- Customs (Advance Rulings) Rules, 2002
- Customs (Appeals) Rules, 1982
- Customs(Import of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 1996
- Specified Goods (Prevention of Illegal Export) Rules, 1969
- Customs (Compounding of Offences) Rules, 2005
- Customs (Settlement of Cases) Rules, 2007
- Notified Goods (Prevention of Illegal Import) Rules, 1969
- Bill of Entry (Electronic Declaration) Regulations, 2011
- Customs (Provisional Duty Assessment) Regulations, 2011
- Customs House Agents Licensing Regulations, 2004

Difference between Rule and Regulations

- (1) *The Central Government is authorized to make the rules and the CBEC is authorized to make the regulations in consistent with this Act.*
- (2) *The powers to make the rules is contained in section 156 whereas the power to make regulations are prescribed under section 157.*
- (3) *Rules may provide for all or any of the following matters, namely:*
 - (a) *the manner of determining the transaction value of the imported goods and export goods under sub-section (1) of section 14;*
 - (b) *the conditions subject to which accessories of, and spare parts and maintenance and repairing implements for, any article shall be chargeable at the same rate of duty as that article;*
 - (c) *the detention and confiscation of goods the importation of which is prohibited and the conditions, if any, to be fulfilled before such detention and confiscation and the information, notices and security to be given and the evidence requisite for the purposes of such detention or confiscation and the mode of verification of such evidence;*
 - (d) *the reimbursement by an informant to any public officer of all expenses and damages incurred in respect of any detention of any goods made on his information and of any proceedings consequent on such detention;*
 - (e) *the information required in respect of any goods mentioned in a shipping bill or bill of export which are not exported or which are exported and are afterwards re-landed;*
 - (f) *the publication, subject to such conditions as may be specified therein, of names and other particulars of persons who have been found guilty of contravention of any of the provisions of this Act or the rules.*
 - (g) *the amount to be paid for compounding and the manner of compounding under sub-section (3) of section 137.*

Whereas regulations may provide for all or any of the following matters, namely:

- (a) *the form of a bill of entry, shipping bill, bill of export, import manifest, import report, export manifest, export report, bill of transhipment, declaration for transhipment boat note and bill of coastal goods;*
- (b) *the manner of export of goods, relinquishment of title to the goods and abandoning them to customs and destruction or rendering of goods commercially valueless in the presence of the proper officer under clause (d) of sub-section (1) of section 26A;*
- (c) *the form and manner of making application for refund of duty under sub-section (2) of section 26A;*
- (d) *the form and manner in which an application for refund shall be made under section 27;*
- (e) *the conditions subject to which the transhipment of all or any goods under sub-section (3) of section 54, the transportation of all or any goods under section 56 and the removal of warehoused goods from one warehouse to another under section 67, may be allowed without payment of duty;*
- (f) *The conditions subject to which any manufacturing process or other operations may be carried on in a warehouse under section 65.*
- (g) *The manner of conducting audit of the assessment of duty of the imported or export goods at the office of the proper officer or the premises of the importer or exporter, as the case may be.*

LEVY OF CUSTOM DUTY

There are three stages in any tax structure, viz., levy, assessment and collection. The basis of levy of tax is specified by the charging section and Customs Act, section 12 (charging section) identifies the person or properties in respect of which tax or duty is to be levied or charged. Under assessment, the liability for payment of duty is quantified and the last stage is the collection of duty which is postpone for later time due to administrative convenience.

As per Section 12, customs duty is imposed on goods imported into or exported out of India as per the rates specified under the Customs Tariff Act, 1975 or any other law. On analysis of Section 12, we derive the following points:

- (i) Customs duty is imposed on goods when such goods are imported into or exported out of India;
- (ii) The levy is subject to other provisions under this Act or any other law;
- (iii) The rates of duty are as specified under the Tariff Act, 1975 or any other law;
- (iv) Even goods belonging to Government are subject to levy, though they may be exempted by some notifications under Section 25.

Custom Tariff Act, 1975 has two schedules. Schedule I prescribe tariff rates for imported goods, known as "Import Tariff" and Schedule II contains tariff for export goods known as "Export Tariff".

TAXABLE EVENT

The basic condition for levy of customs duty is import/export of goods i.e. goods become liable to duty when there is import into or export from India.

- Import means bringing into India from a place outside India [Section 2(23)].
- Export means taking out of India to a place outside India [Section 2(18)].
- "India" includes the territorial waters of India [Section 2(27)]. The limit of the territorial waters is the line every point of which is at a distance of twelve nautical miles from the nearest point of the appropriate baseline.

Though the taxable event is import/export yet it is difficult to determine the exact time of levy. The provision of assessment and collection of duty will be discussed in other parts.

Here in this part, we will discuss the types of duties leviable under Custom tariff Act.

As per section 12, Customs duties are levied on the goods at the rates specified in the schedules to the Customs Tariff Act, 1975. The first schedule prescribed the rates for duty on imports and Second schedule prescribe the rates for duty on exports.

TYPES OF DUTIES UNDER CUSTOMS

There are various types of Customs import duties:

1. BASIC CUSTOM DUTY

It is levied under Section 12 of Customs Act, 1962, and specified under Section 2 of the Customs Tariff Act, 1975. There are different rates for different goods. But the general basic rate is 10%. This basic duty may be exempted by a notification under Section 25. The basic duty may have two rates under the First Schedule to Customs Tariff Act, 1975; viz. standard rates and preferential rates.

Standard and Preferential Rates

Duty at the “Standard rate” is charged where there is no provision for preferential treatment. To be eligible, for the preferential treatment the goods should be the one which are imported from any preferential area covered under the Government of India Agreements for charging preferential rate of duty. The Central Government has the power to increase or reduce or discontinue the preferential rate in respect of any article specified in the First Schedule provided it considers it to be necessary in the public interest. Preferential rate is applied only where the owner of the article (importer) claims at the time of importation, with supporting evidence, that the goods are chargeable with the preferential rate of duty.

2. ADDITIONAL CUSTOM DUTY/COUNTERVAILING DUTY [Section 3(1)]

This is levied under Section 3(1) of the Customs Tariff Act, 1975. The amount is equivalent to the amount of excise duty payable on such goods manufactured in India. In S.K. Patnaik v. State of Orissa, 2000 S.C. it was held that countervailing duty is imposed when excisable articles are imported in order to counter balance the excise duty, which is leviable on similar goods if manufactured in India:

- Countervailing Duty is payable at effective rates.
- When excise duty is exempt/nil rate is applicable on goods imported, no Countervailing Duty is levied (Collector v. J. K. Synthetics 2000 (120) E.L.T. 54(SC)
- Countervailing Duty is leviable even if similar goods are not produced in India.
- Exemption of basic customs duty doesn't automatically mean exemption of Countervailing Duty.
- Countervailing Duty is payable in case of goods leviable under State excise also.
- When the imported goods are valued under Section 4A [valuation based on retail price], or Tariff Values under section 3(2) the amount of Countervailing Duty is calculated accordingly if the goods are sold in retail in India.

Value for calculation of duty: Additional duty is calculated on a value of the imported article determined u/s 14 of the Customs Act and custom duty u/s 12 of the Customs Act and any other law for the time being in force but does not include;

- additional duty referred to in section 3(5)
- The safeguard duty referred to in section 8B and 8C.
- The countervailing duty referred to in section 9
- The anti dumping duty referred to in section 9A.

In case of alcoholic liquor for human consumption imported into India, the Central Government may specify rate of additional duty having regard to the excise duty for the time being leviable on a like alcoholic liquor produced or manufactured in different States or, if a like alcoholic liquor is not produced or manufactured in any State, then, having regard to the excise duty which would be leviable for the time being in different States on the class or description of alcoholic liquor to which such imported alcoholic liquor belongs.

Additional customs duty under section 3(3): Duty of excise leviable on any raw materials, components and ingredients of the same nature as, or similar to those, used in the production or manufacture of any article imported into India.

Rate of duty: Such portion of the excise duty leviable on such raw materials, components and ingredients as, in either case, may be determined by rules made by the Central Government in this behalf.

(3) ADDITIONAL DUTY/SPECIAL ADDITIONAL DUTY (SAD) UNDER SECTION 3(5)

It is levied to offset the effect of sales tax, VAT, local tax or other charges leviable on articles on its sale, purchase or transaction in India. It is leviable on imported goods even if article was not sold in India.

The Central Government may levy additional duty to counter balance the sales tax, value added tax, local tax or any other charges leviable in the like article on its sale, purchase or transportation in India. The rate shall be notified by the Central Government which cannot exceed 4%.

The value of the imported article shall, be the aggregate of the value determined under section 14(1) of the Customs Act, 1962 and any duty of customs chargeable on that article under section 12 of the Customs Act, 1962, and any sum chargeable on that article under any law for the time being in force as an addition to such additional duty of custom under section 3(1), but does not include—

- (a) the duty referred to in sub-section (5);
- (b) the safeguard duty referred to in sections 8B and 8C;
- (c) the countervailing duty referred to in section 9; and
- (d) the anti-dumping duty referred to in section 9A.

Example

Goods imported from UK of having assessable value of ₹50,000. Basic custom duty @10%, rate of additional duty u/s 3(1) is 12% and SAD under section 3(5)@ 4%, Education cess @2% and Secondary and Higher Education Cess @1%. Calculate Total Duty Payable. Also value.

Solution:

	Value (₹)	Duty (₹)
Assessable value	50,000	
Add: BCD@10%	<u>5,000</u>	<u>5,000</u>
Total	55,000	
Add: CVD@12% (12% X 55,000)	<u>6,600</u>	<u>6,600</u>
Total	61,600	11,600
Add: education cess @ 3% on 11,600	<u>348</u>	<u>348</u>
Total	61,948	11948
Add: SAD @4% (4% x 61,948)	<u>2,478</u>	<u>2,478</u>
Total	<u>64,426</u>	<u>14,426</u>

Summary of the Custom duty leviable u/s 3(1), (3) and (5)

Particulars	CVD u/s 3(1)	CVD u/s 3(3)	SAD u/s 3(5)
It is the duty to counter balance	Duty of excise for the time being in force leviable on a like article produced or manufactured in India.	Duty of excise leviable on any raw materials, components and ingredients of the same nature as, or similar to those, used in the production or manufacture of any article imported into India.	Sales tax, value added tax, local tax or any other charges for the time being leviable on a like article on its sale, purchase or transportation in India.

Rate of duty	Rate of excise duty	Rate of excise duty leviable on such raw materials, components and ingredients	Rate notified by the Central Government and shall not exceed 4%.
Computation of Assessable Value	Value under section 14(1)/tariff value determined under section 14(2) (+) Basic custom duty	Value under section 14(1)/tariff value determined under section 14(2) (+) Basic custom duty	Value under section 14(1)/tariff value determined under section 14(2) (+) Basic custom duty (+) CVD under section 3(1) and 3(3) (+) Education cess and Secondary and higher education cess

Important Note: Central Government has exempted Education Cess and Secondary and Higher Education Cess leviable under sub-section (1) of section 3 of the Customs Tariff Act, 1975.

(4) PROTECTIVE DUTY - SECTION 6 & 7 OF THE CUSTOMS TARIFF ACT, 1975

- The protective duties should not be very stiff so as to discourage imports.
- It should be sufficiently attractive to encourage imports to bridge the gap between demand and supply of those articles in the market.
- Section 6 provides that the protective duties are levied by the Central Government upon the recommendation made to it by the Tariff Commission and upon it being satisfied that circumstances exist which render it necessary to take immediate action to provide protection to any industry established in India.
- As per section 7(1), the protective duty shall be effective only upto and inclusive of the date if any, specified in the First Schedule.
- Section 7(2) provides that the Central Government may reduce or increase the duty by notification in the Official Gazette. However, such duty shall be altered only if it is satisfied, after such inquiry as it thinks necessary, that such duty has become ineffective or excessive for the purpose of securing the protection intended to be afforded by it to a similar article manufactured in India.
- If there is any increase in the duty as specified above, then the Central Government is required to place such notification in the Parliament for its approval.
- As per section 7(3), every notification insofar as it relates to increase of such duty, shall be laid before each House of Parliament if it is sitting as soon as may be after the issue of the notification, and if it is not sitting within seven days of its re-assembly, and the Central Government shall seek the approval of Parliament to the notification by a resolution moved within a period of fifteen days beginning with the day on which the notification is so laid before the House of the People. If the Parliament recommends any change in the notification, then the notification shall have effect subject to such changes. However, anything done pursuant to the notification before the recommendation by the Parliament shall be valid.

(5) SAFEGUARD DUTY - SECTION 8B OF CUSTOMS TARIFF ACT, 1975

- The Central Government may impose safeguard duty on specified imported goods, if it is satisfied

that the goods are being imported in large quantities and they are causing serious injury to domestic industry.

However, the safeguard duty shall not be imposed in the following cases:

- Articles originating from developing country, so long as the share of imports of that article from that country does not exceed 3% of the total imports of that article into India.
- Articles originating from more than one developing country, so long as the aggregate of imports from developing countries each with less than 3% import share taken together does not exceed 9% of the total imports of that article into India.
- Unless specifically made applicable in the notification, the articles imported by a 100% EOU or units in a Free Trade Zone or Special Economic Zone.
- The safeguard duty is imposed for the purpose of protecting the interests of any domestic industry in India aiming to make it more competitive.
- As per section 8B (4), the duty imposed under this section shall be in force for a period of 4 years from the date of its imposition.

Central Government may extend the period of such imposition from the date of first imposition provided it is of the opinion that Domestic industry has taken measures to adjust to such injury or as the case may be to such threat and it is necessary that the safeguard duty should continue to be imposed.

However, the total period of levy of safeguard duty is restricted to 10 years.

- Under section 8B(2), the Central Government is also empowered to impose provisional safeguard duty pending determination of the final duty. This provisional duty may be imposed on the basis of preliminary determination that increased imports have caused or threatened to cause serious injury to a domestic industry.

The provisional duty shall be in force for a maximum period of 200 days from the date of its imposition.

If upon final determination, the Central Government is of the opinion that the increased imports have not caused or threatened to cause serious injury to a domestic industry, the duty collected shall be refunded.

- Section 8B(4A) provides that the provisions of the Customs Act, 1962 and the rules and regulations made thereunder, including those relating to the date for determination of rate of duty, assessment, non-levy, short levy, refunds, interest, appeals, offences and penalties shall, as far as may be, apply to the duty chargeable under this section as they apply in relation to duties leviable under that Act.

- ✓ *Safeguard duty is product specific i.e. the safeguard duty is applicable only for certain articles in respect of which it is imposed.*
- ✓ *Every notification issued under this section shall, as soon as may be after it is issued, be laid before each House of Parliament.*
- ✓ *Safeguard duty is in addition to any other duty in respect of such goods levied under this Act or any other law for the time being in force.*
- ✓ *Education Cess and Secondary and Higher Education Cess are not payable on safeguard duty.*

(6) COUNTERVAILING DUTY ON SUBSIDIZED ARTICLES - SECTION 9 OF THE CUSTOMS TARIFF ACT

- Section 9(1) provides that the countervailing duty on subsidized articles is imposed if any country or territory, directly or indirectly, pays or bestows subsidy upon the manufacture or production or exportation of any article. Such subsidy includes subsidy on transportation of such article. Such articles are imported into India. The importation may or may not directly be from the country of manufacture or production. The article, may be in the same condition as when exported from the country of manufacture or production or may be changed in condition by manufacture, production or otherwise.

Subsidy shall be deemed to exist if

- (a) there is financial contribution by a government, or any public body in the exporting or producing country or territory, that is, where -
 - o a government practice involves a direct transfer of funds (including grants, loans and equity infusion), or potential direct transfer of funds or liabilities, or both;
 - o government revenue that is otherwise due is foregone or not collected (including fiscal incentives)
 - o a government provides goods or services other than general infrastructure or purchases goods;
- (b) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions specified in clauses (i) to (iii) above which would normally be vested in the government and the practice in, no real sense, differs from practices normally followed by governments; or
- The amount of countervailing duty shall not exceed the amount of subsidy paid or bestowed as aforesaid.
- Countervailing duty shall not be levied unless it is determined that -
 - (i) The subsidy relates to export performance;
 - (ii) The subsidy relates to the use of domestic goods over imported goods in the export article; or
 - (iii) The subsidy has been conferred on a limited number of persons engaged in manufacturing producing or exporting the article unless such a subsidy is for-
 - o Research activities conducted by or on behalf of such persons engaging in manufacture, production, export;
 - o Assistance to disadvantaged regions within the territory of the exporting country; or
 - o Assistance to promote adaptation of existing facilities to new environmental requirements.
- Unless revoked earlier, the duty imposed under this section shall be in force for a period of 5 years from the date of its imposition.

Central Government may extend the period of such imposition from the date of such extension provided it, in a review, is of the opinion that such cessation is likely to lead to continuation or recurrence of such subsidization and injury.

However, the extension can be for a maximum period of 5 years. If the review is not completed before the expiry of the period of imposition (5 years) then the duty may continue to remain in force pending the outcome of such review for a further period not exceeding 1 year.

- When the determination of the amount of subsidy is pending, the Central Government may impose a provisional countervailing duty not exceeding the amount of such subsidy as provisionally estimated by it.

If the final subsidy determined is less than the subsidy provisionally determined, then the Central Government shall reduce such duty and also refund the excess duty collected.

- As per section 9(4), if the Central Government is of the opinion that
 - The injury to domestic industry, which is difficult to repair, is caused by massive imports in a relatively short period, of the articles benefiting from subsidies and
 - to preclude recurrence of such injury, may by notification levy countervailing duty with retrospective effect;

The retrospective date from which the duty is payable shall not be beyond 90 days from the date of notification.

- The provisions of the Customs Act, 1962 and the rules and regulations made thereunder, including those relating to the date for determination of rate of duty, assessment, non-levy, short levy, refunds, interest, appeals, offences and penalties shall, as far as may be, apply to the duty chargeable under this section as they apply in relation to duties leviable under that Act.

(7) ANTI-DUMPING DUTY (ADD) ON DUMPED ARTICLES - SECTION 9A OF THE CUSTOMS TARIFF ACT, 1975

Where any article is exported by an exporter or producer from any country or territory to India at less than its normal value, then, upon the importation of such article into India, the Central Government may, by notification in the Official Gazette, impose an anti-dumping duty not exceeding the margin of dumping in relation to such article.

Dumping means exporting goods to India, at prices lower than the ones in the domestic market of the exporting country, subject to certain adjustments.

To prevent dumping, the Central Government may levy ADD up to margin of dumping (MOD). MOD is the difference between the normal value and the price charged for exports to India.

Normal value means comparable price in the ordinary course of trade, in the exporting country, after making adjustments to the extent of conditions of sale, taxation, etc.

ANTI DUMPING DUTY CAN BE IMPOSED RETROSPECTIVELY AND PROVISIONALLY

(i) Determination of duty provisionally

The Central Government may, pending the determination in accordance with the provisions of this section and the rules made thereunder of the normal value and the margin of dumping in relation to any article, impose on the importation of such article into India an anti-dumping duty on the basis of a provisional estimate of such value and margin and if such anti-dumping duty exceeds the margin as so determined,-

- the Central Government shall, having regard to such determination and as soon as may be after such determination, reduce such anti-dumping duty; and
- refund shall be made of so much of the antidumping duty which has been collected as is in excess of the anti-dumping duty as so reduced.

(ii) Determination of duty retrospectively:

If the Central Government, in respect of the dumped article under inquiry, is of the opinion that -

- (i) there is a history of dumping which caused injury or that the importer was, or should have been, aware that the exporter practices dumping and that such dumping would cause injury; and
- (ii) the injury is caused by massive dumping of an article imported in a relatively short time which in the light of the timing and the volume of imported article dumped and other circumstances is likely to seriously undermine the remedial effect of the antidumping duty liable to be levied, the Central Government may, by notification in the Official Gazette, levy anti-dumping duty retrospectively from a date prior to the date of imposition of anti-dumping duty but not beyond ninety days from the date of notification, and notwithstanding anything contained in any other law for the time being in force, such duty shall be payable at such rate and from such date as may be specified in the notification.

Period of Duty: The anti-dumping duty imposed under this section shall, unless revoked earlier, cease to have effect on the expiry of five years from the date of such imposition.

However, if the Central Government is of the opinion that the cessation of such duty is likely to lead to continuation or recurrence of dumping and injury, it may, from time to time, extend the period of such imposition for a further period of five years and such further period shall commence from the date of order of such extension.

Where a review initiated before the expiry of the aforesaid period of five years has not come to a conclusion before such expiry, the anti-dumping duty may continue to remain in force pending the outcome of such a review for a further period not exceeding one year.

Important points

- ✓ *Safeguard duty is product specific and anti dumping duty is country specific*
- ✓ *Refund of anti dumping duty is subject to doctrine of unjust enrichment. [Automotive Tyre Manufacturers Association, 2011(SC)]*
- ✓ *Education cess and Secondary and Higher Education cess are not payable on Safeguard duty, Countervailing duty on subsidized articles, anti dumping duty and any other protective duty.*

Computation of Anti Dumping Duty:

Illustration

A commodity is imported into India from a country covered by a notification issued by the Central Government under section 9A of the Customs Tariff Act, 1975. Following particulars are made available:

- *CIF value of the consignment: US \$25,000*
- *Quantity imported : 500 kgs.*
- *Exchange rate applicable : ₹60 = US\$1*
- *Basic customs duty : 10%*

Education and Secondary and Higher education cess as applicable as per the Finance Act. As per the notification, the anti-dumping duty will be equal to the difference between the cost of commodity calculated @ US\$70 per kg and the landed value of the commodity as imported. Calculate the liability on account of normal duties, cess and the anti-dumping duty.

Assume that only 'basic customs duty' (BCD) and education and secondary and higher education cess are payable.

Solution:

Anti dumping duty = Margin of injury.

Margin of injury is the difference between fair market value in India and the landed value of the imported goods.

The fair market value in this case is 35, 000 dollars. (500kg @70 per dollar)

The landed value = Assessable value +BCD with cess.

Assessable value = CIF value +1% landing charges.

	=	25,000+250
	=	25,250
Add: BCD @ 10%	=	2,525
Add: Education Cess @ 3% on 2525	=	75.7
Landed value	=	27,850.75
Margin of injury	=	35,000- 27,850.75
	=	7149.25 US\$
\$ 7149.25 x 60	=	₹ 428,955

Emergency power of Central Government

Under section 8, if the Central Government is satisfied that the export duty leviable thereon should be levied, and that circumstances exist which render it necessary to take immediate action the Central Government may, by notification in the Official Gazette, direct an amendment of the Second Schedule to be made so as to provide for an increase in the export duty leviable or, as the case may be, for the levy of an export duty, on that article.

Similarly, Central Government may, by notification in the Official Gazette, direct an amendment in the First Schedule to be made so as to provide for an increase in the import duty leviable on such article to such extent as it thinks necessary:

IMPORTANT DEFINITIONS

Section 2 of the Customs Act, 1962 contains the definitions of various terms used at several places in the Act. Here, some of the important definitions are reproduced as follows;

- (1) **“Adjudicating Authority”** means any authority competent to pass any order or decision under this Act, but does not include the Board, Commissioner (Appeals) or Appellate Tribunal;
- (2) **“Appellate Tribunal”** means the Customs, Excise and Service Tax Appellate Tribunal constituted under section 129;
- (3) **“Assessment”** includes provisional assessment, self-assessment, re-assessment and any order of assessment in which the duty assessed is nil;
- (4) **“baggage”** includes unaccompanied baggage but does not include motor vehicles [Section 2(3)];

- (5) “**bill of entry**” means a bill of entry referred to in section 46[Section 2(4)];
- (6) “**bill of export**” means a bill of export referred to in section 50[Section 2(5)];
- (7) “**Board**” means the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 (54 of 1963) [Section 2(6)];
- (8) “**coastal goods**” means goods, other than imported goods, transported in a vessel from one port in India to another[Section 2(7)];
- (9) “**dutiable goods**” means any goods which are chargeable to duty and on which duty has not been paid [Section 2(14)];
- (10) “**entry**” in relation to goods means an entry made in a bill of entry, shipping bill or bill of export and includes in the case of goods imported or to be exported by post, the entry referred to in section 82 or the entry made under the regulations made under section 84 [Section 2(16)];
- (11) “**export**”, with its grammatical variations and cognate expressions, means taking out of India to a place outside India [Section 2(18)];
- (12) “**export goods**” means any goods which are to be taken out of India to a place outside India [Section 2(19)];
- (13) “**exporter**”, in relation to any goods at any time between their entry for export and the time when they are exported, includes any owner or any person holding himself out to be the exporter [Section 2(20)];
- (14) “**foreign-going vessel or aircraft**” means any vessel or aircraft for the time being engaged in the carriage of goods or passengers between any port or airport in India and any port or airport outside India, whether touching any intermediate port or airport in India or not, and includes -
- (i) any naval vessel of a foreign Government taking part in any naval exercises;
 - (ii) any vessel engaged in fishing or any other operations outside the territorial waters of India;
 - (iii) any vessel or aircraft proceeding to a place outside India for any purpose whatsoever [Section 2(21)];
- (15) “**goods**” includes -
- (a) vessels, aircrafts and vehicles;
 - (b) stores;
 - (c) baggage;
 - (d) currency and negotiable instruments; and
 - (e) any other kind of movable property [Section 2(22)].
- (16) “**import**”, with its grammatical variations and cognate expressions, means bringing into India from a place outside India [Section 2(23)];
- (17) “**import manifest**” or “**import report**” means the manifest or report required to be delivered under section 30 [Section 2(24)];
- (18) “**imported goods**” means any goods brought into India from a place outside India but does not include goods which have been cleared for home consumption [Section 2(25)];

(19) “**importer**”, in relation to any goods at any time between their importation and the time when they are cleared for home consumption, includes any owner or any person holding himself out to be the importer [Section 2(26)];

(20) “**India**” includes the territorial waters of India [Section 2(27)];

(21) “**Indian customs waters**” means the waters extending into the sea up to the limit of contiguous zone of India under section 5 of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976 (80 of 1976) and includes any bay, gulf, harbour, creek or tidal river [Section 2(28)];

(22) “**person-in-charge**” means -

- (a) in relation to a vessel, the master of the vessel;
- (b) in relation to an aircraft, the commander or pilot-in-charge of the aircraft;
- (c) in relation to a railway train, the conductor, guard or other person having the chief direction of the train;
- (d) in relation to any other conveyance, the driver or other person-in-charge of the conveyance [Section 2(31)].

(23) “**prohibited goods**” means any goods the import or export of which is subject to any prohibition under this Act or any other law for the time being in force but does not include any such goods in respect of which the conditions subject to which the goods are permitted to be imported or exported have been complied with [Section 2(33)];

(24) “**proper officer**”, in relation to any functions to be performed under this Act, means the officer of customs who is assigned those functions by the Board or the Commissioner of Customs [Section 2(34)];

(25) “**shipping bill**” means a shipping bill referred to in section 50 [Section 2(37)];

(26) “**stores**” means goods for use in a vessel or aircraft and includes fuel and spare parts and other articles of equipment, whether or not for immediate fitting; [Section 2(38)];

(27) “**smuggling**”, in relation to any goods, means any act or omission which will render such goods liable to confiscation under section 111 or section 113; [Section 2(39)];

(28) “**tariff value**”, in relation to any goods, means the tariff value fixed in respect thereof under sub-section (2) of section 14 [Section 2(40)];

(29) “**value**”, in relation to any goods, means the value thereof determined in accordance with the provisions of sub-section (1) or sub-section (2) of Section 14 [Section 2(41)];

(30) “**vehicle**” means conveyance of any kind used on land and includes a railway vehicle [Section 2(42)]

(31) “**warehouse**” means a public warehouse appointed under section 57 or a private warehouse licensed under section 58 [Section 2(43)].

(32) “**warehoused goods**” means goods deposited in a warehouse [Section 2(44)];

(33) “**warehousing station**” means a place declared as a warehousing station under section 9. [Section 2(45)];

SELF-TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation)

1. What is the object of levying of duties on Import and Export of goods?
 2. How are the territorial limits of India fixed for the purpose of Import and Export of goods?
 3. What kinds of Import duties are provided under the Customs Act, 1962?

SUGGESTED READING

- (1) Customs Law Manual — *R. K. Jain's*
 - (2) Indirect Taxes Law and Practice — *V.S. Datey*

CUSTOMS LAW

PART II: VALUATION, ASSESSMENT OF IMPORTED AND EXPORT GOODS AND PROCEDURAL ASPECTS

After completion of this lesson, the student will have the clear understanding of;

- Concept of Transaction Value
- Valuation of imported goods and applicable rules
- Valuation of Export goods and applicable rules
- Assessment of imported and export goods
- Provisional assessment
- Remission of duty on pilfered or lost or destroyed goods.
- Levy of duty on goods derelict, wreck, jetsam etc.
- Rules for denaturing or mutilation of goods
- Power of Central Government to grant exemption
- Recovery and refund provisions

INTRODUCTION

The expression “levy”, “assessment” and “collection” have legal import and significance. The term “levy” is superior legislative function, “assessment” a quasi-judicial function and “collection” is an administrative function. In view of Article 265 of the Constitution of India, which lays down that “no tax shall be levied or collected except by authority of law”, it has been held that the words “levy” and “collection” were used in the said Article in a “comprehensive manner and that they are intended to include and envelop the entire process of taxation, commencing from the taxing statute to the taking away of the monies from the pocket of the citizen” [Rayalaseema Constructions v. Deputy Commercial Tax Officer, MR (1959) Madras 382 p. 386].

The following observations of the Punjab High Court in *Hazarimal Kuthalia v. Income-tax Officer*, AIR (1957) Punjab 5, will give an insight to the most important expressions used in taxing statutes:

- (i) To levy a tax means to impose or assess or collect under the authority of law. It is a unilateral act of superior legislative power to declare the subjects and rates of taxation and to authorise the collection to proceed to collect the tax.
- (ii) Assessment is the official determination of liability of a person to pay a particular tax.
- (iii) Collection is the power to gather money for taxes, by enforced payment if necessary.

“These three expressions levy, assessment and collection are of the widest significance and embrace in their broad sweep all the proceedings which can possibly be imagined for raising money by the exercise of the power of taxation from the inception to the conclusion of the proceedings”.

The assessing authorities are thus under obligation in law to assess correctly and properly and should give reasons for their findings in assessment proceedings.

The process of assessment underwent major changes in the Budget 2011, wherein the self assessment scheme was introduced thereby the work of assessment is no more the official determination of liability however, the proper officer can verify and reassess the duty leviable on the goods.

- The Customs Act, 1962, provides vide its section 12, for levy of duties on goods imported or exported from India.
- Customs duty is imposed on goods imported into or exported out of India as per the rates specified under the Customs Tariff Act, 1975.
- Levy of custom duty on ad valorem (i.e. with reference to the value) basis is the predominant mode of levy.
- For this purpose, the value of the imported goods is required to be determined as per provisions of section 14 of the Customs Act, 1962 read with the Customs Valuation (Determination of prices of Imported Goods) Rules, 2007.
- Likewise, in respect of export goods the value is determined as per provisions of section 14 of the Customs Act, 1962 read with the Customs Valuation (Determination of value of Export Goods) Rules, 2007.

VALUATION OF GOODS FOR LEVY OF CUSTOMS DUTY

The method of valuation of goods for both import and export for the purposes of levy of customs duty on the basis of value has been set out under Section 14 of the Customs Act, 1962. Prior to 10.10.2007, the subsection (1) of old section 14 of the Customs Act, 1962 provided that valuation of goods should

be based on the concept of 'deemed value'. Now the concept of deemed value has been retained only in case of residual method under Rule 9 of the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007. However, the Customs Valuation (Determination of Price of Imported Goods) Rules, 1988 provided that the value of the imported goods should be based on the concept of transaction value. The Finance Act, 2007 substituted a new section 14 for old section 14 with an aim to rectify this anomaly. New section 14 speaks of transaction value and has become effective from 10.10.2007.

Consequently, the old Customs Valuation (Determination of Imported Goods) Rules, 1988 (relevant for old section 14) have also been replaced by new Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 and Customs Valuation (Determination of Value of Export Goods) Rules, 2007.

VALUATION OF IMPORTED GOODS

Section 14(1) provides that the value of imported goods shall also include various items of costs and services to the extent provided by the rules. Hence, the value of imported goods shall be computed in accordance with section 14(1) read with the Customs Valuation (Determination of Value of Imported Goods) Rules, 2007.

Let's discuss the valuation rules of import in detail:

CUSTOMS VALUATION (DETERMINATION OF PRICE OF IMPORTED GOODS) RULES, 2007

As per Notification No. 94/2007-Customs (N.T.), dated 13.9.2007, in exercise of the powers conferred by Section 156 read with Section 14 of the Customs Act, 1962 (62 of 1962), the Central Government hereby makes the following rules, namely:

Customs Valuation (Determination of Value of Imported Goods) Rules, 2007

Rule 3	Determination of the method of valuation
Rule 4	Transaction value of identical goods

Rule 5	Transaction value of similar goods
Rule 6	Situation where the above methods cannot be applied
Rule 7	Deductive value method
Rule 8	Computed value

Rule 3 of Import valuation rules provides that the value of the imported goods shall be transaction value adjusted on accordance with rule 10. However, where for any reason the transaction value cannot be determined, or the same is not acceptable for any reason, then, the value shall be determined as per the methods laid down in Rules 4 to 9, which are to be proceeded sequentially.

As per rule 2(g): "**transaction value**" means the value referred to in sub-section (1) of section 14 of the Customs Act, 1962.

As per section 14 of the Customs Act, 1962 the value of imported and export goods shall be the Transaction Value that is the price actually paid or payable;

- when sold for export to India for delivery at the time and place of importation in case of imports and
- when sold for export from India the price for delivery at the time and place of exportation,

where the buyer and seller are not related and price is the sole consideration for the sale subject to such other conditions as "may be specified in the rules" made in this behalf.

The transaction value shall include in addition to the price paid or payable on imported goods any amount paid or payable for costs and services including:

- commissions and brokerage,
- engineering,
- design work,
- Royalties and license fees,
- costs of transportation to the place of importation,
- Insurance,
- loading, unloading and handling charges.

- *The costs and services required to be included in the price actually paid or payable are exhaustive.*
- *"Loading" and "unloading" charges have also been included along with the "handling charges".*
- *The rate of exchange shall be as on the date of submission of bill of entry under section 46 or shipping bill or bill of export is presented under section 50 as the case may be.*

The transaction value of the imported goods, as determined under rule 3(1) shall be acceptable as the value of such goods only if the following conditions are fulfilled [Rule 3(2)]-

(a) there are no restrictions as to the disposition or use of the goods by the buyer other than restrictions which –

- (i) are imposed or required by law or by the public authorities in India; or

- (ii) limit the geographical area in which the goods may be resold; or
- (iii) do not substantially affect the value of the goods;

Among restrictions which would not render a price actually paid or payable unacceptable are restrictions which do not substantially affect the value of the goods.

An example of such restrictions would be the case where a seller requires a buyer of automobiles not to sell or exhibit them prior to a fixed date which represents the beginning of a model year.

- (b) the sale or price is not subject to some condition or consideration for which a value cannot be determined in respect of the goods being valued;

Examples of such conditions: If the sale or price is subject to some condition or consideration for which a value cannot be determined with respect to the goods being valued, the transaction value shall not be acceptable for customs purposes. Some examples of this include-

- (a) The seller establishes the price of the imported goods on condition that the buyer will also buy other goods in specified quantities;
- (b) the price of the imported goods is dependent upon the price or prices at which the buyer of the imported goods sells other goods to the seller of the imported goods;
- (c) the price is established on the basis of a form of payment extraneous to the imported goods, such as where the imported goods are semi-finished goods which have been provided by the seller on condition that he will receive a specified quantity of the finished goods.

However, conditions or considerations relating to the production or marketing of the imported goods shall not result in rejection of the transaction value.

For example, the fact that the buyer furnishes the seller with engineering and plans undertaken in India shall not result in rejection of the transaction value for the purposes of rule 3. Likewise, if the buyer undertakes on his own account, even though by agreement with the seller, activities relating to the marketing of the imported goods, the value of these activities is not part of the value of imported goods nor shall such activities result in rejection of the transaction value.

- (c) no part of the proceeds of any subsequent resale, disposal or use of the goods by the buyer will accrue directly or indirectly to the seller, unless an appropriate adjustment can be made in accordance with the provisions of rule 10 of these rules; and
- (d) the buyer and seller are not related, or where the buyer and seller are related, that transaction value is acceptable for customs purposes under the provisions of rule 3(3).

As per rule 3(3), in the following two cases the transaction value shall be acceptable even if goods are sold to related persons:

- (a) Where the buyer and seller are related, the transaction value shall be accepted provided that the examination of the circumstances of the sale of the imported goods indicates that the relationship did not influence the price.

Where the proper officer of customs has no doubts about the acceptability of the price, it should be accepted without requesting further information from the importer.

For example, the proper officer of customs may have previously examined the relationship, or he may

already have detailed information concerning the buyer and the seller, and may already be satisfied from such examination or information that the relationship did not influence the price.

(b) In a sale between related persons, the transaction value shall be accepted, whenever the importer demonstrates that the declared value of the goods being valued **closely approximates** to one of the following values ascertained at or about the same time.

- (i) the transaction value of identical goods, or of similar goods, in sales to unrelated buyers in India;
- (ii) the deductive value for identical goods or similar goods;
- (iii) the computed value for identical goods or similar goods:

"Unrelated buyers" means buyers who are not related to the seller in any particular case.

However, in applying the values used for comparison, due account shall be taken of demonstrated difference in commercial levels, quantity levels, adjustments in accordance with the provisions of rule 10 and cost incurred by the seller in sales in which he and the buyer are not related;

A number of factors must be taken into consideration in determining whether one value "closely approximates" to another value. These factors include

- the nature of the imported goods,
- the nature of the industry itself,
- the season in which the goods are imported, and
- whether the difference in values is commercially significant.

Since these factors may vary from case to case, it would be impossible to apply a uniform standard such as a fixed percentage, in each case.

For example, a small difference in value in a case involving one type of goods could be unacceptable while a large difference in a case involving another type of goods might be acceptable in determining whether the transaction value closely approximates to the "test" values.

(c) Substitute values shall not be established under the provisions of clause (b) of this sub-rule.

As per rule 3(4), if the value cannot be determined under the provisions of rule 3(1), the value shall be determined by proceeding sequentially through rule 4 to 9.

Before moving to other rules, first discuss the adjustments for costs and services, inclusions and exclusions in accordance with rule 10 as mentioned in Rule 3.

As per rule 2(2), Persons shall be deemed to be "related" only if -

- (i) they are officers or directors of one another's businesses;
- (ii) they are legally recognised partners in business;
- (iii) they are employer and employee;
- (iv) any person directly or indirectly owns, controls or holds five per cent or more of the outstanding voting stock or shares of both of them;
- (v) one of them directly or indirectly controls the other *;
- (vi) both of them are directly or indirectly controlled by a third person;

- (vii) together they directly or indirectly control a third person; or
- (viii) they are members of the same family.

*One person shall be deemed to control another when the former is legally or operationally in a position to exercise restraint or direction over the latter.

Explanation I - The term "person" also includes legal persons.

Explanation II - Persons who are associated in the business of one another in that one is the sole agent or sole distributor or sole concessionaire, howsoever described, of the other shall be deemed to be related for the purpose of these rules, if they fall within the criteria of this sub-rule.

ADJUSTMENTS IN TRANSACTION VALUE (RULE 10)

I. Adjustments specified in Rule 10(1)

In determining the transaction value, there shall be added to the price actually paid or payable for the imported goods, —

- (a) the following to the extent they are incurred by the buyer but are not included in the price actually paid or payable for the imported goods, namely:-

- (i) commission and brokerage, except buying commissions;

*Buying commission refers to fees paid by an importer to his agent for service of representing him abroad in purchase of goods being valued. Commission paid to canalising agent in India is not buying commission – **Hyderabad Industries Ltd. v. UOI (2009) 115 ELT 593 (SC)***

- (ii) the cost of containers imported along with the goods;
- (iii) the cost of packing whether for labour or materials;

Points for consideration regarding Price actually paid or payable

- The price actually paid or payable is the total payment made or to be made by the buyer to or for the benefit of the seller for the imported goods.
- The payment need not necessarily take the form of a transfer of money. Payment may be made by way of letters of credit or negotiable instruments.
- Payment may be made directly or indirectly. **An example of an indirect payment would be the settlement by the buyer, whether in whole or in part, of a debt owed by the seller.**

Activities undertaken by the buyer on his own account, other than those for which an adjustment is provided in rule 10, are not considered to be an indirect payment to the seller, even though they might be regarded as of benefit to the seller. The costs of such activities shall not, therefore, be added to the price actually paid or payable in determining the value of imported goods.

- The value of imported goods shall not include the following charges or costs, provided that they are distinguished from the price actually paid or payable for the imported goods:

- (a) Charges for construction, erection, assembly, maintenance or technical assistance, undertaken after importation on imported goods such as industrial plant, machinery or equipment;
- (b) The cost of transport after importation;
- (c) Duties and taxes in India.

- The price actually paid or payable refers to the price for the imported goods. Thus the flow of dividends or other payments from the buyer to the seller that do not relate to the imported goods are not part of the customs value.

- (b) The value, apportioned as appropriate, of the following goods and services where supplied directly or indirectly by the buyer free of charge or at reduced cost for use in connection with the production and sale for export of imported goods, to the extent not included in the price actually paid or payable, namely:-
 - (i) materials, components, parts and similar items incorporated in the imported goods;
 - (ii) tools, dies, moulds and similar items used in the production of the Imported goods;
 - (iii) materials consumed in the production of the imported goods;
 - (iv) engineering, development, art work, design work, and plans and sketches undertaken elsewhere than in India and necessary for the production of the imported goods;
- (c) royalties and licence fees related to the imported goods that the buyer is required to pay, directly or indirectly, as a condition of the sale of the goods being valued, to the extent that such royalties and fees are not included in the price actually paid or payable.
- (d) The value of any part of the proceeds of any subsequent resale, disposal or use of the imported goods that accrues, directly or indirectly, to the seller;
- (e) all other payments actually made or to be made as a condition of sale of the imported goods, by the buyer to the seller, or by the buyer to a third party to satisfy an obligation of the seller to the extent that such payments are not included in the price actually paid or payable.

Explanation- Where the royalty, licence fee or any other payment for a process, whether patented or otherwise, is includable referred to in clauses (c) and (e), such charges shall be added to the price actually paid or payable for the imported goods, notwithstanding the fact that such goods may be subjected to the said process after importation of such goods.

II. Adjustments specified in Rule 10(2)

The value of the imported goods shall be the value of such goods, for delivery at the time and place of importation and shall include –

- (a) the cost of transport of the imported goods to the place of importation;
- (b) loading, unloading and handling charges associated with the delivery of the imported goods at the place of importation; and
- (c) the cost of insurance actually incurred

The following points shall also be considered while determining the assessable value:

- (i) Where the cost of transport is not ascertainable, such cost shall be 20% of the free on board value of the goods. In the case of goods imported by air, even where the cost of transportation is ascertainable, such cost shall not exceed 20% of free on board value of the goods.
- (ii) where the cost of insurance is not ascertainable, such cost shall be 1.125% of free on board (FOB) value of the goods;
- (iii) loading, unloading and handling charges shall be 1% of the free on board (FOB) value of the goods + the cost of transport + cost of insurance i.e. CIF Value

Computation where FOB value and Cost of Insurance & Transport not ascertainable:

Where the free on board value of the goods is not ascertainable, then

- Costs of transportation shall be 20% of the FOB value of the goods + cost of insurance and
- Cost of insurance shall be 1.125% of the free on board value of the goods + cost of transport.

Other points for consideration

In case of goods imported by sea stuffed in a container for clearance at an Inland Container Depot or Container Freight Station, the cost of freight incurred in the movement of container from the port of entry to the Inland Container Depot or Container Freight Station shall not be included in the cost of transport.

The cost of transport of the imported goods includes the ship demurrage charges on charted vessels, lighterage or barge charges.

Additions to the price actually paid or payable shall be made under this rule on the basis of objective and quantifiable data.

No addition shall be made to the price actually paid or payable in determining the value of the imported goods except as provided for in this rule.

As per the scheme of valuation, transaction value shall be applied to the goods imported into or exported from India. Where it is not possible to apply transaction value, alternative methods have to be applied in sequence. That means first of all, apply Rule 4, where Rule 4 cannot be applied, apply Rule 5 and so on.

DETERMINATION OF TRANSACTION VALUE IN CASE OF IDENTICAL GOODS (RULE 4)

Rule 4(1): If the value cannot be determined under the provisions of rule 3(1), the value shall be the transaction value of the identical goods, which are sold for export to India and imported at or about the same time as the goods being valued.

However, such transaction value shall not be the value of the goods provisionally assessed under section 18 of the Customs Act, 1962.

The transaction value of identical goods will be used in determining the value of imported goods only when such identical goods fulfill the following conditions:

- (i) These goods are in a sale at the same commercial level and
- (ii) These goods are substantially of the same quantity as the goods being valued.

Where these two conditions are not satisfied then the transaction value in a sale of identical goods shall be used under any of the following circumstances;

- sale at a same commercial level but in different quantities or
- sale at a different commercial level but in substantially the same quantity
- sale at a different commercial level and in different quantities.

However, such adjustments shall be made on the basis of demonstrated evidence which clearly establishes the reasonableness and accuracy of the adjustments, whether such adjustment leads to an increase or decrease in the value.

In simple words, while applying rule 4, the proper officer of customs shall, wherever possible, use a sale of identical goods at the same commercial level and in substantially the same quantities as the goods being valued. Where no such sale is found, a sale of identical goods that takes place under any one of the following three conditions may be used:

- (a) a sale at the same commercial level but in different quantities; or
- (b) a sale at a different commercial level but in substantially the same quantities; or
- (c) a sale at a different commercial level and in different quantities.

Having found a sale under any one of these three conditions adjustments will then be made, as the case may be, for:

- (a) *quantity factors only;*
- (b) *commercial level factors only; or*
- (c) *both commercial level and quantity factors.*

Adjustment in the transaction value referred in Rule 10(2) [Rule 4(2)]

Where the costs and charges referred to in sub-rule (2) of rule 10 of these rules are included in the transaction value of identical goods, an adjustment shall be made, if there are significant differences in such costs and charges between the goods being valued and the identical goods in question arising from differences in distances and means of transport.

Transaction value where more than one transaction value found

If more than one transaction value of identical goods is found, the lowest such value shall be used to determine the value of imported goods [Rule 4(3)].

Identical goods [Rule 2(1)(d)]

"Identical goods" means imported goods -

- (i) which are same in all respects, including physical characteristics, quality and reputation as the goods being valued except for minor differences in appearance that do not affect the value of the goods;
- (ii) produced in the country in which the goods being valued were produced; and
- (iii) produced by the same person who produced the goods, or where no such goods are available, goods produced by a different person, but shall not include imported goods where engineering, development work, art work, design work, plan or sketch undertaken in India were completed directly or indirectly by the buyer on these imported goods free of charge or at a reduced cost for use in connection with the production and sale for export of these imported goods;

If the price of such goods is not available, price of goods produced by another manufacturer in the same country can be taken.

TRANSACTION VALUE OF SIMILAR GOODS (RULE 5)

If the value cannot be determined under the provisions of rule 3(1), the value of imported goods shall be the transaction value of similar goods sold for export to India and imported at or about the same time as the goods being valued:

However, such transaction value shall not be the value of the goods provisionally assessed under section 18 of the Customs Act, 1962.

The provisions of rule 4 shall, *mutatis mutandis*, also apply in respect of similar goods.

Similar Goods

Similar Goods [Rule 2(1)(f): "similar goods" means imported goods -

- (i) which although not alike in all respects, have like characteristics and like component materials which enable them to perform the same functions and to be commercially interchangeable with the goods being valued having regard to the quality, reputation and the existence of trade mark;

- (ii) produced in the country in which the goods being valued were produced; and
- (iii) produced by the same person who produced the goods being valued, or where no such goods are available, goods produced by a different person

but shall not include imported goods where engineering, development work, art work, design work, plan or sketch undertaken in India were completed directly or indirectly by the buyer on these imported goods free of charge or at a reduced cost for use in connection with the production and sale for export of these imported goods;

Determination of value where value can not be determined under rules 3, 4 and 5 (rule 6)

If the value of imported goods cannot be determined under the provisions of rules 3, 4 and 5, the value shall be determined under the provisions of rule 7 or, when the value cannot be determined under that rule, under rule 8.

However, at the request of the importer, and with the approval of the proper officer, the order of application of rules 7 and 8 shall be reversed.

DEDUCTIVE VALUE (RULE 7)

Rule 7(1), subject to the provisions of rule 3, if the goods being valued or identical or similar imported goods are sold in India, in the condition as imported at or about the time at which the declaration for determination of value is presented, the value of imported goods shall be based on the unit price at which the imported goods or identical or similar imported goods are sold in the greatest aggregate quantity to persons who are not related to the sellers in India, subject to the following deductions : —

- (i) either the commission usually paid or agreed to be paid or the additions usually made for profits and general expenses in connection with sales in India of imported goods of the same class or kind;
- (ii) the usual costs of transport and insurance and associated costs incurred within India;
- (iii) the customs duties and other taxes payable in India by reason of importation or sale of the goods.

Rule 7(2): If neither the imported goods nor identical nor similar imported goods are sold at or about the same time of importation of the goods being valued, the value of imported goods shall, subject otherwise to the provisions of sub-rule (1), be based on the unit price at which the imported goods or identical or similar imported goods are sold in India, at the earliest date after importation but before the expiry of ninety days after such importation.

Rule 7(3): If neither the imported goods nor identical nor similar imported goods are sold in India in the condition as imported, then, the value shall be based on the unit price at which the imported goods, after further processing, are sold in the greatest aggregate quantity to persons who are not related to the seller in India.

In such determination, due allowance shall be made for the value added by processing and the deductions provided for in items (i) to (iii) of rule 7(1).

The term "unit/price at which goods are sold in the greatest aggregate quantity" means the price at which the greatest number of units is sold in sales to persons who are not related to the persons from whom they buy such goods at the first commercial level after importation at which such sales take place.

Example:

Goods are sold from a price list which grants favourable unit prices for purchases made in larger quantities.

Sale quantity	Unit price	Number of sales	Total quantity sold at each price
1-10 units	100	10 sales of 5 units, 5 sales of 3 units	65
11-25 units	95	5 sales of 11 units	55
Over 25 units	90	1 sale of 30 units, 1 sale of 50 units	80

The greatest number of units sold at a price is 80, therefore, the unit price in the greatest aggregate quantity is 90.

Example:

In the first sale 500 units are sold at a price of 95 currency units each. In the second sale 400 units are sold at a price of 90 currency units each. in this example, the greatest number of units sold at a particular price is 500, therefore, the unit price in the greatest aggregate quantity is 95.

Example:

A third example would be the following situation where various quantities are sold at various prices.

(a) Sales

Sale quantity	Unit price
40 units	100
30 units	90
15 units	100
50 units	95
25 units	105
35 units	90
5 units	100

(b) Totals

Total quantity Sold	Unit price
65	90
50	95
60	100
25	105

In this example, the greatest number of units sold at a particular price is 65, therefore, the unit price in the greatest aggregate quantity is 90.

COMPUTED VALUE (RULE 8)

Subject to the provisions of rule 3, the value of imported goods shall be based on a computed value, which shall consist of the sum of:-

- (a) the cost or value of materials and fabrication or other processing employed in producing the imported goods;
- (b) an amount for profit and general expenses equal to that usually reflected in sales of goods of the

same class or kind as the goods being valued which are made by producers in the country of exportation for export to India;

- (c) the cost or value of all other expenses under rule 10(2).

RESIDUAL METHOD (RULE 9)

Subject to the provisions of rule 3, where the value of imported goods cannot be determined under the provisions of any of the preceding rules, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules and on the basis of data available in India;

However, the value so determined shall not exceed the price at which such or like goods are ordinarily sold or offered for sale for delivery at the time and place of importation in the course of international trade, when the seller or buyer has no interest in the business of other and price is the sole consideration for the sale or offer for sale [Rule 9(1)].

As per rule 9(2), no value shall be determined under the provisions of this rule on the basis of;

- (i) the selling price in India of the goods produced in India;
- (ii) a system which provides for the acceptance for customs purposes of the highest of the two alternative values;
- (iii) the price of the goods on the domestic market of the country of exportation;
- (iv) the cost of production other than computed values which have been determined for identical or similar goods in accordance with the provisions of rule 8;
- (v) the price of the goods for the export to a country other than India;
- (vi) minimum customs values; or
- (vii) arbitrary or fictitious values.

Value of imported goods determined under the provisions of rule 9 should to the greatest extent possible, be based on previously determined customs values.

The methods of valuation to be employed under rule 9 may be those laid down in rules 3 to 8, inclusive, but a reasonable flexibility in the application of such methods would be in conformity with the aims and provisions of rule 9.

Some examples of reasonable flexibility are as follows:

- (a) *Identical goods* - The requirement that the identical goods should be imported at or about the same time as the goods being valued could be flexibly interpreted; identical imported goods produced in a country other than the country of exportation of the goods being valued could be the basis for customs valuation; customs values of identical imported goods already determined under the provisions of rules 7 and 8 could be used.
- (b) *Similar goods* - The requirement that the similar goods should be imported at or about the same time as the goods being valued could be flexibly interpreted; similar imported goods produced in a country other than the country of exportation of the goods being valued could be the basis for customs valuation; customs values of similar imported goods already determined under the provisions of rules 7 and 8 could be used.
- (c) *Deductive method* - The requirement that the goods shall have been sold in the "condition as

"imported" in rule 7(1) could be flexibly interpreted; the ninety days requirement could be administered flexibly.

DECLARATION TO BE FURNISHED BY THE IMPORTER (RULE 11)

The importer or his agent shall furnish -

- (a) a declaration disclosing full and accurate details relating to the value of imported goods; and
 - (b) any other statement, information or document including an invoice of the manufacturer or producer of the imported goods where the goods are imported from or through a person other than the manufacturer or producer, as considered necessary by the proper officer for determination of the value of imported goods under these rules.
- (2) The proper officer of customs has the power to satisfy himself as to the truth or accuracy of any statement, information, document or declaration presented for valuation purposes.
- (3) The provisions of the Customs Act, 1962 (52 of 1962) relating to confiscation, penalty and prosecution shall apply to cases where wrong declaration, information, statement or documents are furnished.

REJECTION OF DECLARED VALUE BY CUSTOMS OFFICER (RULE 12)

When the proper officer has reason to doubt the truth or accuracy of the value declared in relation to any imported goods, he may ask the importer of such goods to furnish further information including documents or other evidence and if, after receiving such further information, or in the absence of a response of such importer, the proper officer still has reasonable doubt about the truth or accuracy of the value so declared, it shall be deemed that the transaction value of such imported goods cannot be determined under the provisions of rule 3(1).

At the request of an importer, the proper officer, shall intimate the importer in writing the grounds for doubting the truth or accuracy of the value declared in relation to goods imported by such importer and provide a reasonable opportunity of being heard, before taking a final decision.

Other points for consideration (Explanation to rule 12)

- (i) This rule by itself does not provide a method for determination of value, it provides a mechanism and procedure for rejection of declared value in cases where there is reasonable doubt that the declared value does not represent the transaction value; where the declared value is rejected, the value shall be determined by proceeding sequentially in accordance with rules 4 to 9.
- (ii) The declared value shall be accepted where the proper officer is satisfied about the truth and accuracy of the declared value after the said enquiry in consultation with the importers.
- (iii) The proper officer shall have the powers to raise doubts on the truth or accuracy of the declared value based on certain reasons which may include -
 - (a) the significantly higher value at which identical or similar goods imported at or about the same time in comparable quantities in a comparable commercial transaction were assessed;
 - (b) the sale involves an abnormal discount or abnormal reduction from the ordinary competitive price;
 - (c) the sale involves special discounts limited to exclusive agents;
 - (d) the mis-declaration of goods in parameters such as description, quality, quantity, country of origin, year of manufacture or production;

- (e) the non declaration of parameters such as brand, grade, specifications that have relevance to value;
- (f) the fraudulent or manipulated documents.

The process of assessment involves value and rate of duty. Value is found out under section 14 and rate of duty is ascertained as per Section 15 and 16 of the Customs Act.

RELEVANT DATE FOR DETERMINATION OF THE RATE OF DUTY AND TARIFF VALUATION (SECTION 15)

Under section 15(1), the rate of duty and tariff valuation, if any, applicable to any *imported goods*, shall be the rate and valuation in force,

- (a) In the case of goods entered for home consumption under section 46: The date on which a bill of entry is presented [Section 15(1)(a)]
- (b) In the case of goods cleared from a warehouse under section 68: The date on which a bill of entry for home consumption is presented [Section 15(1)(b)].
- (c) In the case of any other goods: The date of payment of duty [Section 15(1)(c)].

However, if a bill of entry has been presented before the date of entry inwards of the vessel or the arrival of the aircraft by which the goods are imported, the bill of entry shall be deemed to have been presented on the date of such entry inwards or the arrival, as the case may be [Proviso to section 15(1)].

The provisions of this section shall not apply to baggage and goods imported by post (Section 15(2)).

Illustration

N Ltd. imported a machine by air. Bill of entry was presented on 25-2-2013, entry inwards was granted on 1-3-2013. CIF value \$ 12,000; air freight paid \$ 2400; insurance paid \$ 180

<i>Rate of exchange declared by</i>	<i>As on 25-2-2013</i>	<i>As on 1-3-2013</i>
<i>CBEC</i>	<i>55.25</i>	<i>55.43</i>
<i>RBI</i>	<i>55.62</i>	<i>55.67</i>
<i>BCD applicable</i>	<i>12%</i>	<i>10%</i>

Find out the assessable value and also the appropriate rate of BCD. Make the necessary assumptions.

Solution:

$$\begin{aligned}
 \text{FOB value} &= \text{CIF} - \text{Freight} - \text{insurance} \\
 &= \$12,000 - \$2400 - \$180 \\
 &= \$9420
 \end{aligned}$$

$$\text{FOB Value:} = \$9420$$

$$\text{Add: Freight @ 20\%} = \$1884$$

$$\text{Add: Insurance} = \$180$$

$$\text{CIF Value} = \$11,484$$

Add: Landing charges @1% on CIF 114.84

11598.84 \$

= $11598.84 \times 55.25 = ₹ 640835.91 = ₹ 640836$ (rounded off to nearest rupee)

BCD as per section 15 is 10%

Notes: since the freight exceeds 20% of FOB, it has been calculated by finding out FOB value.

Rate of exchange notified by CBEC on the date of submission of Bill of Entry has been taken.

VALUATION OF EXPORT GOODS

Customs value of export goods, whether liable to ad valorem duty or not is to be determined under Section 14(1) of the Customs Act, 1962 read with Section 2(41) thereof. By virtue of Section 2(41), 'value' in relation to any goods will mean the value thereof determined under Section 14(1).

CUSTOMS VALUATION (DETERMINATION OF VALUE OF EXPORT GOODS) RULES, 2007

Rule 3	Determination of the method of valuation
Rule 4	Determination of export value by comparison
Rule 5	Computed value method
Rule 6	Residual method
Rule 7	Declaration by the exporter
Rule 8	Rejection of declared value

DETERMINATION OF THE METHOD OF VALUATION (RULE 3)

The value of export goods shall be its transaction value. However, the transaction value may be rejected as per the provisions of Rule 8.

As per rule 3(2), the transaction value shall be accepted even where the buyer and seller are related, provided that the relationship has not influenced the price.

If the value cannot be determined under the provisions of Rule 3(1) and (2), the value shall be determined by proceeding sequentially through rules 4 to 6 (Rule 3(3)).

DETERMINATION OF EXPORT VALUE BY COMPARISON (RULE 4)

As per Rule 4(1), the value of the export goods shall be based on the transaction value of "*goods of like kind and quality*" exported at or about the same time to other buyers in the same destination country of importation or in its absence another destination country of importation adjusted in accordance with the provisions of Rule 4(2).

"goods of like kind and quality" means export goods which are identical or similar in physical characteristics, quality and reputation as the goods being valued, and perform the same functions or are commercially interchangeable with the goods being valued, produced by the same person or a different person;

"Transaction value" means the value of export goods within the meaning of sub-section (1) of section 14 of the Customs Act, 1962 (52 of 1962).

For the purposes of these rules, persons shall be deemed to be "related" only if -

- (i) they are officers or directors of one another's businesses;
- (ii) they are legally recognised partners in business;
- (iii) they are employer and employee;
- (iv) any person directly or indirectly owns, controls or holds five per cent or more of the outstanding voting stock or shares of both of them;
- (v) one of them directly or indirectly controls the other;
- (vi) both of them are directly or indirectly controlled by a third person;
- (vii) together they directly or indirectly control a third person; or
- (viii) they are members of the same family.

Explanation I. - The term "person" also includes legal persons.

Explanation II. - Persons who are associated in the business of one another in that one is the sole agent or sole distributor or sole concessionaire, howsoever described, of the other shall be deemed to be related for the purpose of these rules, if they fall within the criteria of this sub-rule.

Adjustments under Rule 4(2):

In determining the value of export goods under sub-rule (1), the proper officer shall make such adjustments as appear to him reasonable, taking into consideration the relevant factors, including-

- (i) difference in the dates of exportation,
- (ii) difference in commercial levels and quantity levels,
- (iii) difference in composition, quality and design between the goods to be assessed and the goods with which they are being compared,
- (iv) difference in domestic freight and insurance charges depending on the place of exportation.

COMPUTED VALUE METHOD (RULE 5)

If the value cannot be determined under rule 4, it shall be based on a computed value, which shall include the following:-

- (a) cost of production , manufacture or processing of export goods;
- (b) charges, if any, for the design or brand;
- (c) an amount towards profit.

Computed value = Cost of production + Charges if any for design or brand +An amount towards profit.

The board has clarified that while determining the value under this rule, the proper officer shall give due consideration to the cost certificate issued by the Cost Accountant or Chartered Accountant or Government approved valuer, as produced by the exporter.

RESIDUAL METHOD (RULE 6)

Subject to the provisions of rule 3, where the value of the export goods cannot be determined under the provisions of rules 4 and 5, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules provided that local market price of the export goods may not be the only basis for determining the value of export goods.

DECLARATION BY THE EXPORTER (RULE 7)

The exporter shall furnish a declaration relating to the value of export goods in the manner specified in this behalf.

REJECTION OF DECLARED VALUE (RULE 8)

As per rule 8(1), when the proper officer has reason to doubt the truth or accuracy of the value declared in relation to any export goods, he may ask the exporter of such goods to furnish further information including documents or other evidence and if, after receiving such further information, or in the absence of a response of such exporter, the proper officer still has reasonable doubt about the truth or accuracy of the value so declared, the transaction value shall be deemed to have not been determined in accordance with Rule 3(1).

Under rule 8(2), at the request of an exporter, the proper officer shall intimate the exporter in writing the ground for doubting the truth or accuracy of the value declared in relation to the export goods by such exporter and provide a reasonable opportunity of being heard, before taking a final decision under Rule 8(1).

OTHER IMPORTANT POINTS

- (i) This rule by itself does not provide a method for determination of value, it provides a mechanism and procedure for rejection of declared value in cases where there is reasonable doubt that the declared value does not represent the transaction value; where the declared value is rejected, the value shall be determined by proceeding sequentially in accordance with rules 4 to 6.
- (ii) The declared value shall be accepted where the proper officer is satisfied about the truth or accuracy of the declared value after the said enquiry in consultation with the exporter.
- (iii) The proper officer shall have the powers to raise doubts on the declared value based on certain reasons which may include –
 - (a) the significant variation in value at which goods of like kind and quality exported at or about the same time in comparable quantities in a comparable commercial transaction were assessed.
 - (b) the significantly higher value compared to the market value of goods of like kind and quality at the time of export.
 - (c) the mis-declaration of goods in parameters such as description, quality, quantity, year of manufacture or production.

RELEVANT DATE FOR DETERMINATION OF RATE OF DUTY AND TARIFF VALUATION OF EXPORT GOODS (SECTION 16)

As per section 16(1), the rate of duty and tariff valuation, if any, applicable to any export goods, shall be the rate and valuation in force, -

- (a) in the case of goods entered for export under section 50, on the date on which the proper officer makes an order permitting clearance and loading of the goods for exportation under section 51.
- (b) in the case of any other goods, on the date of payment of duty.

The provisions of this section shall not apply to baggage and goods exported by post [Section 16(2)].

Illustration:

<i>CIF value:</i>	<i>10,000 US Dollars</i>
<i>Exchange rate notified by RBI :</i>	<i>₹ 46/-</i>

Exchange rate notified by CBEC: ₹45/-

The following rates of customs are applicable to the consignment

- (1) Basic customs duty: 10%
- (2) CVD 16%. Same goods manufactured in India attract exemption by 6%
- (3) Education cess is payable at 2%.
- (4) Special CVC is payable at applicable rates.

Find out:

- (i) Assessable value
- (ii) Duties payable
- (iii) Eligibility of CENVAT Credit

Solution:

CIF Value	10,000	USD
Add: Landing charges @ 1% of CIF Value	<u>100</u>	
Assessable value	10,100	USD
₹45 x 10,100 = 4,54,500		
	₹	Duty (₹)
Assessable Value	4,54,500	
(1) Add: B.C.D. @10%	<u>45,450</u>	45,450
	4,99,950	
(2) Add: CVC @10% (16% – 6%)	<u>49,995</u>	49,995
	5,49,945	
(3) Add: Edu. Cess @2% on ₹95,445	<u>2,863</u>	<u>2,863</u>
Total Value before Spl. CVD	5,52,808	98,308
Add: Spl. CVD @4% on 5,52,808	<u>22,112</u>	<u>22,112</u>
Total	<u>5,74,920</u>	<u>1,20,420</u>

Total CENVAT Credit available to the buyer is ₹49,995 + ₹22,112 + ₹72,107

$$= ₹72,107$$

Note: Education cess on CVD is exempt with effect from 17.03.12 vide Notification No. 13 & 14/2012 (T)

Illustration

Import by Air

CIF Value: 1,000 Euros.

Freight: 300 Euros

Insurance: 15 Euros

Find the assessable value.

The exchange rate notified by CBEC as on the date of submission of Bill of Entry was ₹70 per euro.

Solution:

Since the freight charges cannot exceed 20% of FOB value, it is necessary to find out FOB value.

		Euros
FOB value:		1,000
Less: Freight	300	
Insurance	<u>15</u>	315
FOB		685
Add: Freight @20% on 685		137
Add: Insurance	<u>15</u>	837.00
Add: Landing charges @1%		<u>8.37</u>
		<u>845.37</u>

Assessable value in Indian Rupees = ₹70 x 845.37 = ₹59,176/- (rounded off)

ASSESSMENT OF DUTY

Section 17 of the Customs Act, prescribes the method for assessment of duty. For example, under Sub-section (1), after an importer has entered any imported goods or an exporter has entered any export goods, the importer and exporter self assess the duty if any leviable on such goods. As per sub-section 2 the self assessed goods may be verified, examined or tested by the proper officer.

Section 17 reads as follows:

- (1) An importer entering any imported goods under section 46, or an exporter entering any export goods under section 50, shall, save as otherwise provided in section 85, self-assess the duty, if any, leviable on such goods.
- (2) The proper officer may verify the self-assessment of such goods and for this purpose, examine or test any imported goods or export goods or such part thereof as may be necessary.
- (3) For verification of self-assessment under sub-section (2), the proper officer may require the importer, exporter or any other person to produce any contract, broker's note, insurance policy, catalogue or other document, whereby the duty leviable on the imported goods or export goods, as the case may be, can be ascertained, and to furnish any information required for such ascertainment which is in his power to produce or furnish, and thereupon, the importer, exporter or such other person shall produce such document or furnish such information.
- (4) Where it is found on verification, examination or testing of the goods or otherwise that the self-assessment is not done correctly, the proper officer may, without prejudice to any other action which may be taken under this Act, re-assess the duty leviable on such goods.
- (5) Where any re-assessment done under sub-section (4) is contrary to the self-assessment 25 done by the importer or exporter regarding valuation of goods, classification, exemption or concessions of duty availed consequent to any notification issued therefore under this Act and in cases other than those where the importer or exporter, as the case may be, confirms his acceptance of the said re-assessment in writing, the proper officer shall pass a speaking order on the re-assessment, within fifteen days from the date of re-assessment of the bill of entry or the shipping bill, as the case may be.
- (6) Where re-assessment has not been done or a speaking order has not been passed on re-assessment,

the proper officer may audit the assessment of duty of the imported goods or export goods at his office or at the premises of the importer or exporter, as may be expedient, in such manner as may be prescribed.

PROVISIONAL ASSESSMENT OF DUTY [SECTION 18]

Notwithstanding anything contained in this Act but without prejudice to the provisions of section 46,

- (a) where the importer or exporter is unable to make self-assessment under section 17(1) and makes a request in writing to the proper officer for assessment; or
- (b) where the proper officer deems it necessary to subject any imported goods or export goods to any chemical or other test; or
- (c) where the importer or exporter has produced all the necessary documents and furnished full information but the proper officer deems it necessary to make further enquiry; or
- (d) where necessary documents have not been produced or information has not been furnished and the proper officer deems it necessary to make further enquiry,

the proper officer may direct that the duty leviable on such goods be assessed provisionally if the importer or the exporter, as the case may be, furnishes such security as the proper officer deems fit for the payment of the deficiency, if any, between the duty as may be finally assessed and the duty provisionally assessed [Section 18(1)].

When the duty leviable on such goods is assessed finally or reassessed by the proper officer in accordance with the provisions of this Act, then -

- (a) in the case of goods cleared for home consumption or exportation, the amount paid shall be adjusted against the duty finally assessed and if the amount so paid falls short of, or is in excess of the duty finally assessed, the importer or the exporter of the goods shall pay the deficiency or be entitled to a refund, as the case may be;
- (b) in the case of warehoused goods, the proper officer may, where the duty finally assessed or reassessed, as the case may be, is in excess of the duty provisionally assessed, require the importer to execute a bond, binding himself in a sum equal to twice the amount of the excess duty [Section 18(2)].

The importer or exporter shall be liable to pay interest, on any amount payable to the Central Government, consequent to the final assessment order or re-assessment order, at the rate fixed by the Central Government under section 28AB from the first day of the month in which the duty is provisionally assessed till the date of payment thereof [Section 18(3)].

Subject to the section 18(5), if any refundable amount referred to in clause (a) of section 18(2) is not refunded under that sub-section within three months from the date of assessment of duty finally or reassessment of duty, as the case may be, there shall be paid an interest on such un-refunded amount at such rate fixed by the Central Government under section 27A till the date of refund of such amount [Section 18(4)].

As per section 18(5), the amount of duty refundable under section 18(2) and the interest under section 18(4), if any, shall, instead of being credited to the Fund, be paid to the importer or the exporter, as the case may be, if such amount is relatable to.

- (a) the duty and interest, if any, paid on such duty paid by the importer, or the exporter, as the case may be, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;

- (b) the duty and interest, if any, paid on such duty on imports made by an individual for his personal use;
- (c) the duty and interest, if any, paid on such duty borne by the buyer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- (d) the export duty as specified in section 26;
- (e) drawback of duty payable under sections 74 and 75.

DETERMINATION OF DUTY WHERE GOODS CONSIST OF ARTICLES LIABLE TO DIFFERENT RATES OF DUTY (SECTION 19)

Except as otherwise provided in any law for the time being in force, where goods consist of a set of articles, duty shall be calculated as follows:-

- (a) articles liable to duty with reference to quantity shall be chargeable to that duty;
- (b) articles liable to duty with reference to value shall, if they are liable to duty at the same rate, be chargeable to duty at that rate, and if they are liable to duty at different rates, be chargeable to duty at the highest of such rates;
- (c) articles not liable to duty shall be chargeable to duty at the rate at which articles liable to duty with reference to value are liable under clause (b) :

However,

- (a) accessories of, and spare parts or maintenance and repairing implements for, any article which satisfy the conditions specified in the rules made in this behalf shall be chargeable at the same rate of duty as that article;
- (b) if the importer produces evidence to the satisfaction of the proper officer or the evidence is available regarding the value of any of the articles liable to different rates of duty, such article shall be chargeable to duty separately at the rate applicable to it.

RE-IMPORTATION OF GOODS (SECTION 20)

When goods are re-imported into India, after exportation there from, such goods are liable to duty and are subject to all the conditions and restrictions, if any, to which goods of the like kind and value are liable or subject, on the importation thereof. The provisions relating to these matters are found in Section 20 of the Customs Act, 1962.

Section 20, which got amended by Finance Act, 1994, (w.e.f. 13.5.1994), until this amendment, covered only goods produced and manufactured in India, when imported after being exported from India and provided that these will be chargeable to customs duty and subject to the same conditions as goods imported afresh. However, the amendment has extended the applicability of the provisions of this section to all goods imported into India after being exported and not only those goods which are manufactured or produced in India. Thus, goods imported after being exported in bond would henceforth be chargeable to normal customs duty. The amended Section 20 reads as under:

If goods are imported into India after exportation there from, such goods shall be liable to duty and be subject to all the conditions and restrictions, if any, to which goods of the like kind and value are liable or subject, on the importation thereof.

Notification Nos. 94/96 and 158/95 provide for certain relaxations for reimported goods.

DUTY ON PILFERED GOODS (SECTION 13)

If any imported goods are

- pilfered after the unloading thereof and
- before the proper officer has made an order for clearance for home consumption or deposit in a warehouse,
- the importer shall not be liable to pay the duty leviable on such goods except where such goods are restored to the importer after pilferage.

As per section 45(3), if any imported goods are pilfered after unloading thereof in a customs area while in the custody of a person approved by the Commissioner u/s 45(1), that person shall be liable to pay duty on such goods at the rate prevailing on the date of delivery of an import manifest or an import report to the proper officer u/s 30 for the arrival of the conveyance in which the said goods were carried.

GOODS DERELICT, WRECK, ETC. (SECTION 21)

Section 21 lays down that all goods, derelict, jetsam, flotsam and wreck brought or coming into India, shall be dealt with as if they were imported into India, unless it be shown to the satisfaction of the proper officer that they are entitled to be admitted duty free under this Act.

“Derelict” is a term applied to any property, whether vessel or cargo, left or abandoned in open sea by persons in charge of it without any hope of recovering or intention of returning to it.

“Jetsam” is where the goods are thrown into the sea with a view to lighten the ship in order to prevent it from sinking.

“Flotsam” is where the goods having been at sea in a ship, are separated from it by some peril. The property in this case is not renounced by the owner by throwing them overboard and the owner is entitled to recover the possession.

“Wreck” refers to the property cast ashore within the ebb and flow of the tide after shipwreck. The property involved may be a ship, a cargo or portion thereof.

ABATEMENT OF DUTY ON DAMAGED OR DETERIORATED GOODS (SECTION 22)

If any goods are found damaged and are examined by customs authority for that purpose on an application made therefor, the duty can be charged only on the goods which are serviceable or on the reduced value as may be determined by customs authority. Provisions in this regard have been made under Section 22 of the Customs Act, 1962.

Under Section 22, there is allowed abatement of duty on damaged or deteriorated goods under Sub-section (1), where it is shown to the satisfaction of the Assistant/Deputy Commissioner of Customs—

- (a) that any imported goods had been damaged or had deteriorated at any time before or during the unloading of the goods in India; or
- (b) that any imported goods, other than warehoused goods, had been damaged at any time after the unloading thereof in India but before their examination under Section 17, on account of any accident not due to any wilful act, negligence or default of the importer, his employee or agent; or
- (c) that any warehoused goods have been damaged at any time before clearance for home consumption on account of any accident not due to any wilful act, negligence or default of the owner his employee or agent.

Such goods are chargeable to duty in accordance with the provisions of Sub-section (2).

Sub-section (2) lays down that the duty to be charged on the goods referred above shall bear the same proportion to the duty chargeable on the goods before the damage or deterioration which the value of the damaged or deteriorated goods bear to the value of the goods before the damage or deterioration.

Under Sub-section (3), the value of damaged or deteriorated goods may, be ascertained by either of the following methods at the option of the owner, viz.:

- (a) the value of such goods may be ascertained by the proper officer, or
- (b) such goods may be sold by the proper officer by public auction or by tender, or with the consent of the owner in any other manner and the gross proceeds shall be deemed to be the value of such goods.

REMISSION OF DUTY ON LOST, DESTROYED OR ABANDONED GOODS (SECTION 23)

Where any goods are lost or destroyed, except by way of pilferage, whether totally or partially, even after the "out of charge" is signed but before they are physically removed from customs area, the owner is entitled for remission of duty on such goods.

Further, an owner of goods can surrender the title to the goods to customs before an order for home consumption has been made and no duty need be paid on such goods.

Section 23 relates to remission of duty on lost, destroyed or abandoned goods. It reads as follows:

- (1) Without prejudice to the provisions of Section 13, where it is shown to the satisfaction of the Assistant/Deputy Commissioner of Customs that any imported goods have been lost otherwise than as a result of pilferage or destroyed, at any time before clearance for home consumption, the Assistant/Deputy Commissioner of Customs shall remit the duty on such goods.
- (2) The owner of any imported goods may, at any time before an order for clearance of goods for home consumption under Section 47 or an order for permitting the deposit of goods in a warehouse under Section 60 has been made, relinquish his title to the goods and thereupon he shall not be liable to pay the duty thereon".

Provided that the owner of any such imported goods shall not be allowed to relinquish his title to such goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

DENATURING OR MUTILATION OF GOODS (SECTION 24)

The Central Government may make rules for permitting at the request of the owner the denaturing or mutilation of imported goods which are ordinarily used for more than one purpose so as to render them unfit for one or more of such purposes; and where any goods are so denatured or mutilated they shall be chargeable to duty at such rate as would be applicable if the goods had been imported in the denatured or mutilated form.

Denaturing is connected with liquid items and mutilation is associated with solid items. After the process of mutilation or denaturing, the goods are classified as per the latest condition and the lower rate as applicable after mutilation or denaturing will be taken for assessment. This provision is importer friendly and this benefit is given to encourage him to undertake the mutilation/ denaturing process in India.

For example, you may import pure ethyl alcohol attracting 150% of BCD and you may denature it by adding copper sulphate. Then after denaturing it is classified as denatured ethyl alcohol which attracts only 30% BCD.

POWER TO GRANT EXEMPTION FROM DUTY (SECTION 25)

Under the section, exemptions are of two kinds. One type which is in common use, is under Sub-section (1), in public interest, where there is a general exemption in respect of any article or class of articles. Such exemptions may be absolute or subject to certain conditions specified in the relevant notifications. Under Sub-section (2), the exemptions granted may be applicable to specific cases and these will be by a special order. These have to be done in respect of any goods of strategic or secret nature or for charitable purpose, which are stated in such order.

Notifications exempting goods under Sub-section (1) have to be laid before Parliament, as soon as may be, after their issue and the Parliament may amend or reject them. This shows that such notifications are in exercise of 'sovereignty' i.e. legislative powers. On the other hand, special order under Sub-section (2) is an executive order because it is not required to be published and it grants exemption specifically and not generally.

Sub-sections (4) and (5), puts it beyond doubt that every exemption notification shall, unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette. It is also provided that there shall be a statutory obligation for publication of notifications by the Directorate of Publicity and Public Relations and for their sale to the public. The Directorate of Publicity and Public Relations is required to publish the notifications on the date on which the notification is issued by the Government. If, however, the notification is issued but Public Relations can publish the notification on a date not later than the date from which the notification is to be effective. The notifications shall however, also continue to be published in the Gazette of India, as usual.

This amendment has been made in order to do away with the practical problem caused about effective date of notifications by recent Supreme Court judgement in *Collectors v. New Tobacco Co.* (1998) 97 E.L.T. 388 (S.C.).

However, exemptions granted under Section 25(1) of the Customs Act, can operate only in respect of such duty as is specifically mentioned in the particular notification. Thus, a notification exempting goods from the levy of basic customs duty can not by itself exempt such goods from the levy of countervailing duty or additional duty leviable under the Tariff Act nor can exemption from levy of countervailing duty or additional duty, wholly or partially, result in exemption of the goods from the levy of basic customs duty, wholly or partially.

In order to obtain a keen insight and to understand the philosophy or rationale underlying the grant of exemptions it is pertinent to note the explanation given by the Ministry of Finance to the Public Accounts Committee of the Lok Sabha, which had made some observations regarding manner and reasons underlying grant of exemptions from customs duty [PAC (5th Lok Sabha) (1974-75), 135th Report p. 55]. The Ministry of Finance had explained that the exemptions from customs duty were granted for one or more of the following reasons:

- (i) in accordance with the General Agreement on Trade and Tariff certain concessions agreed to by India have to be implemented through exemption notifications;
- (ii) in cases, where indigenously manufactured finished products using imported raw materials are placed at a disadvantageous position vis-a-vis imported finished products on account of high incidence of import duties leviable on imported articles, the industries concerned have to be given tariff assistance by bringing down, through exemption notifications, the import duties applicable in the case of imported raw materials to a level necessary for the removal of the disadvantages;
- (iii) in cases where component/raw materials required for the initial setting up, assembly or manufacture

of machinery/finished product are assessable to duty at a higher rate than what is leviable on the machinery/finished product, the tariff anomaly has to be set right through exemption notifications, equalising the two rates;

- (iv) certain raw materials/semi-finished products are imported for producing finished products which are to be exported later. In such cases, exemptions from import duties have to be given in the interest of export promotion; and
- (v) some exemptions have to be given on humanitarian grounds like relief, rehabilitation, and repatriation of Indians, etc.

Accordingly, exemptions of the types enumerated above are given under Section 25(1) of the Customs Act, 1962. Ad hoc exemptions, however, are given under Sub-section (2) of the said section only under the designed conditions after the amendment of this sub-section by the Finance Act, 1999. The amended policy guidelines issued by the Finance Ministry for grant of such exemption are reproduced below:

POLICY GUIDELINES FOR AD HOC EXEMPTIONS UNDER SECTION 25(2)

In supersession of the Office Memorandum dated 8th October, 1996, the Finance Minister has approved the following guidelines for consideration of request for exemption from customs duty under Section 25(2) of the Customs Act, 1962 as amended by the Finance Act, 1999:

- (a) Imports of secret goods by Government.
- (b) Imports for India's defence needs relating only to military hardware and software or for R&D units under the DRDO may be allowed free of duty.
- (c) Imports by Central Policy Organisation for equipping their forces may be allowed free of duty.
- (d) State Police Organisations may be allowed to import free of duty equipments required for anti-subversion, anti-terrorism and intelligence work.
- (e) Imports by Charitable Institutions which are providing all their services free where the imports are required for use in hospitals, educational institutions, etc., may be allowed free of duty.

The imports by these charitable organisations should fulfill the following conditions:

- (i) The imports should be received as donations or gifts and the donor should be known institution, but not an individual, say a society or a foundation. No payment for imports should be involved.
 - (ii) The recipient should also be an institution/organisation, but not an individual, which is registered as charitable organisation.
 - (iii) The said organisation/institution should be providing services, such as running hospitals, educational institutions etc., on either 'free' or 'no loss or no profit' basis.
 - (iv) The charitable nature of the organisation and the fact of rendering services on 'free' or 'no loss no profit' basis should be certified by the concerned district authorities.
 - (v) The organisation/institution should certify that the goods under import are for its use and provide an undertaking to the effect that they would fulfill the conditions.
2. All ad hoc exemptions from duty to non-governmental organisation will be issued subject to the conditions that the imported goods will not be put to any commercial use and will not be sold, gifted or parted by the importer in any manner without the prior permission of the Ministry of Finance. The imported goods will be kept available for inspection by Customs Officers.

3. Import of goods which are not covered in any of the categories mentioned in para 1 will not be considered for grant of ad hoc exemptions under Section 25(2) of the Customs Act, 1962.

Section 25 read as follows:

(1) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by notification in the Official Gazette, exempt generally either absolutely or subject to such conditions (to be fulfilled before or after clearance) as may be specified in the notification goods of any specified description from the whole or any part of duty of customs leviable thereon.

(2) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by special order in each case, exempt from the payment of duty, under circumstances of an exceptional nature to be stated in such order, any goods on which duty is leviable.

(2A) The Central Government may, if it considers it necessary or expedient so to do for the purpose of clarifying the scope or applicability of any notification issued under sub-section (1) or order issued under subsection (2), insert an explanation in such notification or order, as the case may be, by notification in the Official Gazette, at any time within one year of issue of the notification under sub-section (1) or order under sub-section (2), and every such explanation shall have effect as if it had always been the part of the first such notification or order, as the case may be.

(3) An exemption under sub-section (1) or sub-section (2) in respect of any goods from any part of the duty of customs leviable thereon (the duty of customs leviable thereon being hereinafter referred to as the statutory duty) may be granted by providing for the levy of a duty on such goods at a rate expressed in a form or method different from the form or method in which the statutory duty is leviable and any exemption granted in relation to any goods in the manner provided in this sub-section shall have effect subject to the condition that the duty of customs chargeable on such goods shall in no case exceed the statutory duty.

Explanation. - “Form or method”, in relation to a rate of duty of customs, means the basis, namely, valuation, weight, number, length, area, volume or other measure with reference to which the duty is leviable.

(4) Every notification issued under sub-section (1) or sub-section (2A) shall, -

- (a) unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette;
- (b) also be published and offered for sale on the date of its issue by the Directorate of Publicity and Public Relations of the Board, New Delhi.

(5) Notwithstanding anything contained in sub-section (4), where a notification comes into force on a date later than the date of its issue, the same shall be published and offered for sale by the said Directorate of Publicity and Public Relations on a date on or before the date on which the said notification comes into force.

(6) Notwithstanding anything contained in this Act, no duty shall be collected if the amount of duty leviable is equal to, or less than, one hundred rupees.

REFUND AND RECOVERY PROVISIONS (SECTION 26 TO 28D)

REFUND OF EXPORT DUTY IN CERTAIN CASES (SECTION 26)

Where on the exportation of any goods any duty has been paid, such duty shall be refunded to the person by whom or on whose behalf it was paid, if -

- (a) the goods are returned to such person otherwise than by way of re-sale;
- (b) the goods are re-imported within one year from the date of exportation; and

- (c) an application for refund of such duty is made before the expiry of six months from the date on which the proper officer makes an order for the clearance of the goods.

REFUND OF IMPORT DUTY IN CERTAIN CASES (SECTION 26A)

Section 26A has been introduced by the Finance Act, 2009 for providing refund of import duty in certain cases.

As per sub section 1 of section 26A, where on the importation of any goods capable of being easily identified as such imported goods, any duty has been paid on clearance of such goods for home consumption, such duty shall be refunded to the person by whom or on whose behalf it was paid, if;

- (a) the goods are found to be defective or otherwise not in conformity with the specifications agreed upon between the importer and the supplier of goods:
However, no duty shall be refunded where the goods have been worked, repaired or used after importation except where such use was indispensable to discover the defects or non-conformity with the specifications.
- (b) the goods are identified to the satisfaction of the Assistant Commissioner of Customs or Deputy Commissioner of Customs as the goods which were imported;
- (c) the importer does not claim drawback under any other provisions of this Act; and
- (d) (i) the goods are exported; or
(ii) the importer relinquishes his title to the goods and abandons them to customs; or
(iii) such goods are destroyed or rendered commercially valueless in the presence of the proper officer, in such manner as may be prescribed and within a period not exceeding thirty days from the date on which the proper officer makes an order for the clearance of imported goods for home consumption under section 47:

The period of thirty days may be extended by the Commissioner of Customs for a period not exceeding three months where sufficient cause being shown (first proviso to section 26A).

However, these provisions shall not apply to the goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force (Second proviso to section 26A).

An application for refund of duty shall be made before the expiry of six months from the relevant date in such form and in such manner as may be prescribed [section 26(2)].

"Relevant date" means,—

- (a) *in cases where the goods are exported out of India, the date on which the proper officer makes an order permitting clearance and loading of goods for exportation under section 51;*
- (b) *in cases where the title to the goods is relinquished, the date of such relinquishment;*
- (c) *in cases where the goods are destroyed or rendered commercially valueless, the date of such destruction or rendering of goods commercially valueless.*

As per section 26(3), no refund shall be allowed in respect of perishable goods and goods which have exceeded their shelf life or their recommended storage-before-use period.

Section 26(4) provides that the Board may, by notification in the Official Gazette, specify any other condition subject to which the refund under sub-section (1) may be allowed.

CLAIM FOR REFUND OF DUTY (SECTION 27)

- (1) Section 27 of the Customs Act deals with the refund of the duty. As per this section—
- Any person who has paid the duty or interest or who has borne the incidence of duty or interest can claim refund of duty by way of application.
 - The application for refund is to be made to the Assistant Commissioner of customs or Deputy Commissioner of customs.
 - The application should be made before the expiry of one year from the date of payment of such duty or interest. However the limitation period of one year shall not apply where duty or interest is paid under protest.
 - The application should be accompanied by such documentary or other evidence to establish that the amount of duty or interest in relation to which such refund is claimed was collected from, or paid by him and incidence of such amount is not transferred to any other person.

The period of one year shall be computed from the following date:

- | | |
|---|---|
| <p>(1) <i>Where goods are exempt from payment of duty — by a special order under Sub-section (2) of Section 25</i></p> | <p><i>Date of issue of such order.</i></p> |
| <p>(2) <i>Duty becomes refundable because of judgement, decree, order or direction of appellate authority, appellate tribunal, or court</i></p> | <p><i>Date of such judgement decree, order or direction</i></p> |
| <p>(3) <i>Duty is paid provisionally under Section 18</i></p> | <p><i>Date of adjustment of duty after final assessment</i></p> |

Where the amount of refund claimed is less than rupees one hundred the same shall not be refunded.

(2) If, on receipt of any such application, the Assistant/Deputy Commissioner of Customs is satisfied that the whole or any part of the duty and interest, if any, paid on such duty paid by the applicant is refundable, he may make an order accordingly and the amount so determined shall be credited to the Fund:

Provided that the amount of duty and interest, if any, paid on such duty as determined by the Assistant/Deputy Commissioner of Customs under the foregoing provisions of this sub-section shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to:

- the duty and interest, if any, paid on such duty paid by the importer or exporter, as the case may be, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- the duty and interest, if any, paid on such duty on imports made by an individual for his personal use;
- the duty and interest, if any, paid on such duty borne by the buyer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;
- the export duty as specified in Section 26;
- drawback of duty payable under Sections 74 and 75;
- the duty and interest if any, paid on such duty borne by any other such class of applicants as the

Central Government may, by notification in the Official Gazette, specify:

Provided further that no notification under clause (f) of the first proviso shall be issued unless in the opinion of the Central Government the incidence of duty and interest, if any, paid on such duty has not been passed on by the persons concerned to any other person.

(3) Notwithstanding anything to the contrary contained in any judgement, decree, order or direction of the Appellate Tribunal or any Court or in any other provision of this Act or the regulations made thereunder or any other law for the time being in force, no refund shall be made except as provided in Sub-section (2).

(4) Every notification under clause (f) of the first proviso to Sub-section (2) shall be laid before each House of Parliament, if it is sitting, as soon as may be after the issue of the notification, and if it is not sitting, within seven days of its re-assembly, and the Central Government shall seek the approval of Parliament to the notification by a resolution moved within a period of fifteen days beginning with the day on which the notification is so laid before the House of the People and if Parliament makes any modification in the notification or directs that the notification should cease to have effect, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be, but without prejudice to the validity of anything previously done thereunder.

(5) For the removal of doubts, it is hereby declared that any notification issued under clause (f) of the first proviso to Sub-section (2), including any such notification approved or modified under Sub-section (4), may be rescinded by the Central Government at any time by notification in the Official Gazette.

INTEREST ON DELAYED REFUNDS (SECTION 27A)

Section 27A incorporated in the Customs Act by the Finance Act, 1995 (w.e.f. 26.5.95) provide for payment of interest on refunds of duty which is not paid to the applicant within three months from the date of receipt of application under Sub-section (1) of Section 27.

It has also been provided that in case where appellate remedies are resorted to either by the Department or by the assessee, the refund finally payable shall bear interest for the period starting from the date immediately after the expiry of three months from the date of receipt of applications under Sub-section (1) of Section 27 till the date of refund of duty. It may be specifically noted that:

- (a) interest will be paid only on the amount of duty which is finally held to be refunded.

Example: in case the assessee has claimed a refund of ₹60,000/- the Assistant/Deputy Commissioner allows a refund of ₹10,000/- and on appeal the amount decided to be refunded is ₹30,000/- then the interest would be payable on the amount finally decided to be refunded viz. ₹30,000/- for the period commencing from the expiry of three months from the date of the refund application till its payment. Conversely, if the Assistant/Deputy Commissioner has determined the amount due as refund at ₹30,000/- which on appeal by the Department is reduced to ₹10,000/- interest would be payable for the aforesaid period only on the amount of ₹10,000/-;

- (b) the interest will be paid at the rate to be fixed by the Central Government by issue of Gazette Notification as simple interest, Interest on interest is not payable;
- (c) no interest is to be paid on any refund of fines or penalties; the provision has been made for payment of interest only on delayed refund of duty amounts;
- (d) it is to be clearly noted that interest if any would be payable on the amount of duty to be refunded arising only from proceedings initiated under Section 27 i.e. where an application for refund has been filed.

RECOVERY OF DUTIES NOT LEVIED OR SHORT-LEVIED OR ERRONEOUSLY REFUNDED (SECTION 28)

Where any duty has not been levied or has been short-levied or erroneously refunded, or any interest has not been paid or erroneously refunded, for—

- (1) any reason other than the reason of collusion or any willful mis-statement or suppression of facts then the proper officer shall within one year from the relevant date serve notice on the person chargeable with duty or interest requiring him to show cause why he should not pay the amount specified in the notice.

However the person chargeable with duty or interest may pay before the service of notice any amount of duty along with interest or interest on the basis of—

- (i) his own ascertainment of such duty or
- (ii) the duty ascertained by the proper officer

and inform the proper officer of such payment in writing, who, on receipt of such information shall not serve any notice in respect of duty or interest so paid. However proper officer can issue notice for the remaining amount.

The proper officer shall not serve such show cause notice, where the amount involved is less than rupees one hundred.

- (2) the reason of—
 - (i) collusion; or
 - (ii) any willful mis-statement; or
 - (iii) suppression of facts,

by the importer or exporter or the agent or employee of the importer or exporter, the proper officer shall within 5 years from the relevant date, serve notice on the person chargeable with duty or interest which has not been so levied or which has been so short-levied or short-paid or to whom the refund has erroneously been made, requiring him to show cause why he should not pay the amount specified in the notice.

However the person may pay the duty in full or in part, as may be accepted by him, and the interest payable thereon under Section 28AA and the penalty equal to twenty-five percent of the duty specified in the notice or the duty so accepted by that person, within thirty days of the receipt of notice and inform the proper officer about the payment in writing.

The proper officer then determine the amount of duty or interest and on determination, if proper officer is of the opinion—

- (i) that the duty with interest and penalty has been paid in full, then, the proceedings in respect of such person or other person to whom the notice is served, under Sub-section (1) or Sub-section (4) shall, without prejudice to the provision of Section 135, 135H and 140 be deemed to be conclusive as to the matters stated therein; or
- (ii) that the duty with interest and penalty paid falls short of the amount actually payable, then proper officer shall proceed to issue the notice in respect of the amount which falls short within a period of one year from the date of receipt of information about such payment.

The proper officer shall determine the amount within—

- (a) six months from the date of notice in respect of cases where duty has not been levied or has been short-levied or erroneously refunded, or any interest has been paid, part-paid or erroneously refunded, for any reason other than the reason of collusion or any willful mis-stated or suppression of facts.
- (b) within one year from the date of notice in respect of cases where reasons for non-levy, short leavy or erroneous refund are collusion, any willful misstatement or suppression of facts.

“relevant date” means—

- (a) in a case where duty is not levied, or interest is not charged, the date on which the proper officer makes an order for the clearance of goods;
- (b) in a case where duty is provisionally assessed under Section 18, the date of adjustment of duty after the final assessment thereof;
- (c) in a case where duty or interest has been erroneously refunded, the date of such refund;
- (d) in any other case, the date of payment of duty or interest.

POWER NOT TO RECOVER DUTIES NOT LEVIED OR SHORT-LEVIED AS A RESULT OF GENERAL PRACTICE (SECTION 28A)

(1) Notwithstanding anything contained in this Act, if the Central Government is satisfied –

- (a) that a practice was, or is, generally prevalent regarding levy of duty (including non-levy thereof) on any goods imported into, or exported from, India; and
- (b) that such goods were, or are, liable –
 - (i) to duty, in cases where according to the said practice the duty was not, or is not being, levied, or
 - (ii) to a higher amount of duty than what was, or is being, levied, according to the said practice, then,

the Central Government may, by notification in the Official Gazette, direct that the whole of the duty payable on such goods, or, as the case may be, the duty in excess of that payable on such goods, but for the said practice, shall not be required to be paid in respect of the goods on which the duty was not, or is not being, levied, or was, or is being, short-levied, in accordance with the said practice.

(2) Where any notification under sub-section (1) in respect of any goods has been issued, the whole of the duty paid on such goods, or, as the case may be, the duty paid in excess of that payable on such goods, which would not have been paid if the said notification had been in force, shall be dealt with in accordance with the provisions of sub-section (2) of section 27:

However, where the person is claiming the refund of such duty or, as the case may be, excess duty, makes an application in this behalf to the Assistant Commissioner of Customs or Deputy Commissioner of Customs, in the form referred to in sub-section (1) of section 27, before the expiry of six months from the date of issue of the said notification.

INTEREST ON DELAYED PAYMENT OF DUTY (SECTION 28AA)

(1) Notwithstanding anything contained in any judgment, decree, order or direction of any court, Appellate Tribunal or any authority or in any other provision of this Act or the rules made there under, the person, who is liable to pay duty in accordance with the provisions of section 28, shall, in addition to such duty, be liable to

pay interest, if any, at the rate fixed under sub-section (2), whether such payment is made voluntarily or after determination of the duty under that section.

(2) Interest at such rate not below ten per cent. and not exceeding thirty-six per cent per annum, as the Central Government may, by notification in the Official Gazette, fix, shall be paid by the person liable to pay duty in terms of section 28 and such interest shall be calculated from the first day of the month succeeding the month in which the duty ought to have been paid or from the date of such erroneous refund, as the case may be, up to the date of payment of such duty.

(3) Notwithstanding anything contained in sub-section (1), no interest shall be payable where,—

- (a) the duty becomes payable consequent to the issue of an order, instruction or direction by the Board under section 151A; and
- (b) such amount of duty is voluntarily paid in full, within forty-five days from the date of issue of such order, instruction or direction, without reserving any right to appeal against the said payment at any subsequent stage of such payment.”.

RECOVERY OF DUTIES IN CERTAIN CASES (SECTION 28AAA)

Section 28AAA(1) Instruments obtained by collusion, willful misstatement or suppression of facts for the purpose of Customs Act/Foreign Trade (Development & Regulation) Act and utilized will be subject to action for recovery.

The amount is recoverable from the person to whom such instrument was issued.

As per Proviso to Section 28AAA(1), importer may also be subject to action under Section 28.

Explanation 1: Instrument means any scrip, authorization, license or certificate issued under FTDR Act with respect to a reward scheme under Foreign Trade Policy.

Explanation 2: This section is applicable to utilization made after the Finance Act, 2012 became effective.

(2) Interest @18% is also payable from the date of utilization of the instrument till the date of recovery.

(3) A show cause notice has to be issued by proper officer for recovery.

- A 30 days time shall be given to respond and make representation if any.
- Order should be passed by giving opportunity of being heard for recovery of duty, interest or both.
- The amount in the order passed shall not exceed the amount specified in the show cause notice.
- The amount shall be paid within 30 days of receiving the order.
- Interest is payable whether specifically mentioned in the order or not.

(4) An order need not be passed separately if an order has been passed under Section 28.

(5) The amount if not paid within 30 days, shall be recovered under Section 142(1).

Difference between refund under Section 26, 26A and 27

Section 26 deals with refund of export duty which is rarity. It is granted under the conditions that the goods same goods by same party were re-imported within 1 year and an application was made for refund within 6 months. Moreover, doctrine of unjust enrichment is not applicable to this refund.

Section 26A on the other hand is the refund of import duty in special cases though limitation period to claim

the refund under this section is also 6 months.

Section 27(1) deals with general cases of refund (other than those under Sections 26 and 26A) and it is more procedural in nature. Under this, limitation period is 1 year for all claimants. Moreover, refund in majority of cases is subject to doctrine of unjust enrichment.

Section 27(2) gives the list of instances where refund is possible. Those instances include both the cases which undergo the test of doctrine of unjust enrichment and which do not require to take the test.

Duties collected from the buyer to be deposited with the Central Government (Section 28B)

(1) Notwithstanding anything to the contrary contained in any order or direction of the Appellate Tribunal, National Tax Tribunal or any Court or in any other provision of this Act or the regulations made thereunder, every person who is liable to pay duty under this Act and has collected any amount in excess of the duty assessed or determined or paid on any goods under this Act from the buyer of such goods in any manner as representing duty of customs, shall forthwith pay the amount so collected to the credit of the Central Government.

(1A) Every person who has collected any amount in excess of the duty assessed or determined or paid on any goods or has collected any amount as representing duty of customs on any goods which are wholly exempt or are chargeable to nil rate of duty from any person in any manner, shall forthwith pay the amount so collected to the credit of the Central Government.

(2) Where any amount is required to be paid to the credit of the Central Government under sub-section (1) or sub-section (1A), as the case may be, and which has not been so paid, the proper officer may serve on the person liable to pay such amount, a notice requiring him to show cause why he should not pay the amount, as specified in the notice to the credit of the Central Government.

(3) The proper officer shall, after considering the representation, if any, made by the person on whom the notice is served under sub-section (2), determine the amount due from such person (not being in excess of the amount specified in the notice) and thereupon such person shall pay the amount so determined.

(4) The amount paid to the credit of the Central Government under sub-section (1) or sub-section (1A) or sub-section (3) as the case may be, shall be adjusted against the duty payable by the person on finalisation of assessment or any other proceeding for determination of the duty relating to the goods referred to in subsection (1) or sub-section (1A).

(5) Where any surplus is left after the adjustment made under sub-section (4), the amount of such surplus shall either be credited to the Fund or, as the case may be, refunded to the person who has borne the incidence of such amount, in accordance with the provisions of section 27 and such person may make an application under that section in such cases within six months from the date of the public notice to be issued by the Assistant Commissioner of Customs for the refund of such surplus amount.

Provisional attachment to protect revenue in certain cases (Section 28BA)

(1) Where, during the pendency of any proceeding under section 28 or section 28B, the proper officer is of the opinion that for the purpose of protecting the interests of revenue, it is necessary so to do, he may, with the previous approval of the Commissioner of Customs, by order in writing, attach provisionally any property belonging to the person on whom notice is served under sub-section (1) of section 28 or sub-section (4) of section 28, as the case may be, in accordance with the rules made in this behalf under section 142.

(2) Every such provisional attachment shall cease to have effect after the expiry of a period of six months

from the date of the order made under sub-section (1):

Provided that the Chief Commissioner of Customs may, for reasons to be recorded in writing, extend the aforesaid period by such further period or periods as he thinks fit, so, however, that the total period of extension shall not in any case exceed two years :

Provided further that where an application for settlement of case under section 127B is made to the Settlement Commission, the period commencing from the date on which such application is made and ending with the date on which an order under sub-section (1) of section 127C is made shall be excluded from the period specified in the preceding proviso.

PRICE OF GOODS TO INDICATE THE AMOUNT OF DUTY PAID THEREON (SECTION 28C)

Notwithstanding anything contained in this Act or any other law for the time being in force, every person who is liable to pay duty on any goods shall, at the time of clearance of the goods, prominently indicate in all the documents relating to assessment, sales invoice, and other like documents, the amount of such duty which will form part of the price at which such goods are to be sold.

PRESUMPTION THAT INCIDENCE OF DUTY HAS BEEN PASSED ON TO THE BUYER (SECTION 28D)

Every person who has paid the duty on any goods under this Act shall, unless the contrary is proved by him, be deemed to have passed on the full incidence of such duty to the buyer of such goods.

SELF TEST QUESTION

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. How is the 'assessment value' of imported goods determined for the purpose of levying of Import duties under the Customs Act, 1962? Is there any change in the law in this regard in the recent past? Explain.
2. What cost elements constitute the value of imported goods for the purpose of assessable value?
3. What is the concept of 'Transaction Value' introduced through the newly enacted Valuation Rules, 1988?
4. Under what circumstances 'Transaction Value' may not be accepted for valuation of imported goods?
5. How is the custom duty levied in case imported goods are pilfered before clearance?
6. How is the rate of Duty and Tariff Valuation determined in case of imported goods?
7. How is the rate of duty determined in case of export goods?
8. What is the procedure of assessment of Customs Duty in case of import and export of goods?
9. What are the circumstances under which customs duties may be assessed provisionally?
10. What is the procedure and conditions of provisional assessment of customs duties?
11. How is the customs duty determined where goods consist of articles liable to different rates of duty?
12. State the circumstances when the abatement of customs duty may be allowed under the Act?
13. What are the provisions with regard to levying of duties of customs on goods found derelict, wreck,

etc. on importation?

14. What are the provisions of Customs Act, 1962 with regard to remission of duty on lost, destroyed or abandoned goods ?
15. What are the provisions of Customs Act, 1962 with regard to grant of exemption from custom duty ?
16. State the circumstances and reasons for providing of exemptions from customs duty under the Customs Act, 1962.
17. Who has the power to grant exemptions of customs duty and what kinds of exemptions can be granted within the provisions of Customs Act, 1962?
18. State the circumstances under which refund of export duty is permitted.
29. When can the claim for refund of customs duty be made and what is the procedure for the same?
20. What are the provisions under the Customs Act, 1962 regarding recoveries of duties with retrospective effect? State the circumstances and reasons.

SUGGESTED READINGS:

- (1) Customs Law Manual — *R.K. Jains*
- (2) *Indirect Taxes Law and Practice* — *V.S. Datey*

CUSTOMS LAW

PART III: ARRIVAL OR DEPARTURE AND CLEARANCE OF IMPORTED OR EXPORT GOODS

After completion of this part the students will

- Understand the procedure for import and export of goods
- Be familiar with the types of documents used for import and exports
- Have clear understanding of the arrival or departure provisions

INTRODUCTION

Goods are imported in India or exported from India through sea, air or land. Goods can come through post parcel or as baggage with passengers. Different procedures are there for import and export of goods by different mode of transportation.

The word conveyance is defined in section 2(9), “Conveyance includes a vessel, an aircraft and a vehicle”.

As per section 2(42), the word “Vehicle” means conveyance of any kind used on land and includes a railway vehicle.

Here in this part, the provisions pertaining to import or export of goods through vessel or aircraft are discussed and the import and export of goods through post or as baggage with passenger are discussed in other parts.

This part is divided in three sub-parts namely; -

- I. Provisions relating to conveyances carrying imported or export goods (Section 29 to 43)
- II. Clearance of Imported goods and Export goods (Sections 44 to 51)
- III. Goods in transit (Section 52 to 56)

SECTION S	CONTENT OF THE SECTIONS
Sections 29-36	Arrival of Ship/ Air Craft and unloading of Imported Goods
Sections 37-38	Powers of The Proper Officer to Board Conveyances and Ask Questions
Sections 39-43	Duties and Responsibilities of Conveyances in Export of Goods
Sections 44-49	Clearance of Imported Goods
Sections 50-51	Clearance of Export Goods
Sections 52- 56	Transit And Transshipment of Goods

I. PROVISIONS RELATING TO CONVEYANCES CARRYING IMPORTED OR EXPORT GOODS

Chapter VI contains section 29 to 43 prescribing the provisions for arrival or departure of goods by vessel or aircraft. Let's understand some important terms before moving to the main procedure of arrival or departure

of goods.

1. **“Customs airport”** means any airport appointed under clause (a) of section 7 to be a customs airport [Section 2(10)].
2. **“Customs area”** means the area of a customs station and includes any area in which imported goods or export goods are ordinarily kept before clearance by Customs Authorities [Section 2(11)].
3. **“Customs port”** means any port appointed under clause (a) of section 7 to be a customs port and includes a place appointed under clause (aa) of that section to be an inland container depot [Section 2(12)].
4. **“Customs station”** means any customs port, customs airport or land customs station [Section 2(13)].

Section 7 of the Customs Act, 1962 envisages that the unloading/clearance of imported goods and loading/clearance of export goods shall be allowed only at places notified by the Board as Customs ports or Customs airports or Land Customs Stations or Inland Container Depots. At each such Customs ports or airport, the Commissioner of Customs is empowered to approve proper places for the unloading and loading of goods, and specify the limits of such Customs area under section 8 of the Act. It is further provided vide Section 29 ibid that the person in charge of the vessel or an aircraft shall not call or land at any place other than a Customs port/airport, except in cases of emergencies.

5. **‘Import’** with its grammatical variations and cognate expressions, means bringing into India from a place outside India [Section 2(23)].
6. **‘Import goods’** means “any goods brought into India from a place outside India but does not include goods which have been cleared for home consumption” [Section 2(25)].
7. **‘Importer’** in relation to any goods at any time between their importation and the time when they are cleared for home consumption, includes any owner or any person holding himself out to be the importer [Section 2(26)].
8. **‘Import Manifest’** or **‘import report’** means the manifest or report required to be delivered under section 30. [Section 2(24)]
9. **“Person-in-charge”** means, -
 - (a) in relation to a vessel, the master of the vessel;
 - (b) in relation to an aircraft, the commander or pilot-in-charge of the aircraft;
 - (c) in relation to a railway train, the conductor, guard or other person having the chief direction of the train;
 - (d) in relation to any other conveyance, the driver or other person-in-charge of the conveyance; [Section 2(31)]
10. **“Land Customs Station”** means any place appointed under clause (b) of section 7 to be a land customs station [Section 2(29)]

The organisations which play vital roles in the clearance of Import cargo are:

- (i) **The Steamer Agents/Airline Companies** as the case may be (who are “appointed by the person in charge of a conveyance and who represent to any officer of Customs as an agent, (Section 148) who transport the goods to India, (carriers).
- (ii) **The Port Trust Authorities or International Airport Authorities of India (IAAI)** (in case of air

consignments) who are approved by the Commissioner of Customs as Custodians of Imported Cargo, (Section 45) who act as bailees and are responsible for the receipt, storage, custody and delivery of the goods, after the customs formalities are complied with by the Importers.

- (iii) **The Custom House Agents** now renamed as customs brokers, who are licenced by the Commissioner of Customs (Section 45) to carry on business as an agent relating to the entry or departure of a conveyance or the Import or the Export of goods at any customs station. The agents are licensed in accordance with the Custom House Agents (Licensing) Regulations which inter alia provide for:
 - (a) the validity of any such licence, the fees payable therefore;
 - (b) the qualification of persons who may apply for a licence;
 - (c) the qualifications of persons to be employed by a licensee to assist him in his work as an agent;
 - (d) the restrictions and conditions subject to which a licence may be granted.
- (iv) **The Custom Houses** comprising particularly Customs Officers of the Appraising Department, viz., the Deputy Commissioner, Appraisers, Examiners and supporting ministerial staff as well as various other units in the Customs House.

PROVISIONS RELATING TO ARRIVAL OR DEPARTURE OF GOODS

(1) NOT TO LAND AT ANY PLACE OTHER THAN CUSTOMS PORT OR CUSTOMS AIRPORT (SECTION 29)

The person-in-charge of a vessel or an aircraft entering India from any place outside India shall not cause or permit the vessel or aircraft to call or land at any place other than a customs port or a customs airport -

- (a) for the first time after arrival in India; or
- (b) at any time while it is carrying passengers or cargo brought in that vessel or aircraft as the case may be, unless permitted by the Board.

However, any vessel or aircraft which is compelled by accident, stress of weather or other unavoidable cause to call or land at a place other than a customs port or customs airport but the person-in-charge of any such vessel or aircraft –

- (a) shall immediately report the arrival of the vessel or the landing of the aircraft to the nearest customs officer or the officer-in-charge of a police station and shall on demand produce to him the log book belonging to the vessel or the aircraft;
- (b) shall not without the consent of any such officer permit any goods carried in the vessel or the aircraft to be unloaded from, or any of the crew or passengers to depart from the vicinity of, the vessel or the aircraft; and
- (c) shall comply with any directions given by any such officer with respect to any such goods, and no passenger or member of the crew shall, without the consent of any such officer, leave the immediate vicinity of the vessel or the aircraft :

The departure of any crew or passengers shall not be prohibited from the vicinity of, or the removal of goods from, the vessel or aircraft where the departure or removal is necessary for reasons of health, safety or the preservation of life or property.

(2) DELIVERY OF IMPORT MANIFEST (SECTION 30)

In accordance with Section 30 of the Customs Act, 1962 the person in charge (Master / Agent) of the vessel

or an aircraft has to deliver an import manifest electronically (an import report in case of a vehicle), prior to arrival in the case of a vessel and an aircraft or within 12 hours of arrival in case of a vehicle in the prescribed form. The time limit for filing the manifest is extendable on showing sufficient cause, but otherwise a penalty not exceeding ₹50,000/- can be imposed on account of any delay. A person filing the manifest/report declarations under this section has to declare the truthfulness of contents, which has legal consequences.

Now, it is mandatory to file Import manifest electronically. However, the commissioner of Customs may in cases where it is not feasible to deliver import manifest by presenting electronically allow the same to be delivered in any other manner.

The forms of the Import Manifest are prescribed in the Import Manifest (Vessels) Regulations, 1971 and Import Manifest (Air Craft) Regulations, 1976, which have been made under Section 157 of the Customs Act, 1962.

In practice the Steamer Agents, acting on behalf of the Master of the Ship, file the Import Manifest in the Import Department of the Customs House before the actual arrival of the ship at the port. This is done to enable the importers to file their documents and complete as much of the Customs formalities as possible, before the arrival of the ship so that, there is no delay in the clearance of the cargo when they are landed. Proviso (a) to Section 30(1) of the Customs Act provides for presentation of Import Manifest even before the arrival of the Steamer.

The Import Manifest is required to be delivered in duplicate in the Import Department with full particulars in respect of the following:

- (i) General declaration (giving information mainly about the vessel, its Master, number of crew, passengers);
- (ii) Cargo declaration;
- (iii) Vessel's Store List; and
- (iv) List of private property in the possession of Master, Officers and Crew.

Separate particulars are required to be furnished in the cargo declaration in respect of:

- (a) Cargo to be landed;
- (b) Same Bottom Cargo - 'Cargo in transit';
- (c) Cargo for transhipment; and
- (d) Unaccompanied Baggage.

The information required to be given with regard to the Cargo to be landed at the Port, includes identifying particulars (marks and numbers) of the packages etc. The Serial Number in the Manifest for a particular consignment is known as the "Line number" of the Manifest. The documents filed for clearance bear this line number for purposes of co-relating the clearance documents with the entry in the Manifest.

Steamer Agents acting on behalf of the master of the vessel are accountable to the department for all the goods mentioned in the Manifest as for import into India (Section 116 of the Customs Act, 1962). Steamer Agents in this regard file undertaking(s) and also a guarantee to pay any penalty that may be imposed under Section 116, if they do not account for, to the satisfaction of the Assistant Commissioner of Customs, or for their failure to unload any goods or for any deficiency in the unloaded goods.

In regard to Air Consignments, the 'Import Cargo Manifest' is presented in Triplicate or Quadruplicate by the persons concerned immediately on landing of the Aircraft and the cargo as detailed in the Manifest as

intended for landing are checked by the Customs Officers (Import Freight Officers of the Preventive formation) and then made over for custody to the International Airports Authority of India (IAAI).

The cargo manifest is then sent to the Customs Appraising Formation (Air Cargo Complex) by the Import Freight Officer.

Now, E-filing of import manifest is mandatory.

Assignment of Import Rotation Number

On receipt of the Import Manifest in the Import Department of the Customs House and at the Air Cargo Complex as the case may be, it is checked and an import rotation number assigned to the vessel/Aircraft for the particular voyage. The rotation number is the running serial number for each calendar year in respect of the Manifest filed.

(3) IMPORTED GOODS NOT TO BE UNLOADED FROM VESSEL UNTIL ENTRY INWARDS GRANTED (SECTION 31)

The master of a vessel shall not permit the unloading of any imported goods until an order has been given by the proper officer granting entry inwards to such vessel.

No order under sub-section (1) shall be given until an import manifest has been delivered or the proper officer is satisfied that there was sufficient cause for not delivering it.

Nothing in this section shall apply to the unloading of baggage accompanying a passenger or a member of the crew, mail bags, animals, perishable goods and hazardous goods.

(4) IMPORTED GOODS NOT TO BE UNLOADED UNLESS MENTIONED IN IMPORT MANIFEST OR IMPORT REPORT (SECTION 32)

No imported goods required to be mentioned under the regulations in an import manifest or import report shall, except with the permission of the proper officer, be unloaded at any customs station unless they are specified in such manifest or report for being unloaded at that customs station.

(5) UNLOADING AND LOADING OF GOODS AT APPROVED PLACES ONLY (SECTION 33)

Except with the permission of the proper officer, no imported goods shall be unloaded, and no export goods shall be loaded, at any place other than a place approved under clause (a) of section 8 for the unloading or loading of such goods.

(6) GOODS NOT TO BE UNLOADED OR LOADED EXCEPT UNDER SUPERVISION OF CUSTOMS OFFICER (SECTION 34)

Imported goods shall not be unloaded from, and export goods shall not be loaded on, any conveyance except under the supervision of the proper officer.

However, the Board may, by notification in the Official Gazette, give general permission and the proper officer may in any particular case give special permission, for any goods or class of goods to be unloaded or loaded without the supervision of the proper officer.

(7) RESTRICTIONS ON GOODS BEING WATER-BORNE (SECTION 35)

No imported goods shall be water-borne for being landed from any vessel and no export goods which are not

accompanied by a shipping bill, shall be water-borne for being shipped, unless the goods are accompanied by a boat-note in the prescribed form.

However, the Board may, by notification in the Official Gazette, give general permission, and the proper officer may in any particular case give special permission, for any goods or any class of goods to be water-borne without being accompanied by a boat-note.

(8) RESTRICTIONS ON UNLOADING AND LOADING OF GOODS ON HOLIDAYS, ETC. (SECTION 36)

No imported goods shall be unloaded from, and no export goods shall be loaded on, any conveyance on any Sunday or on any holiday observed by the Customs Department or on any other day after the working hours, except after giving the prescribed notice and on payment of the prescribed fees, if any.

However, no fees shall be levied for the unloading and loading of baggage accompanying a passenger or a member of the crew, and mail bags.

(9) POWER TO BOARD CONVEYANCES (SECTION 37)

The proper officer may, at any time, board any conveyance carrying imported goods or export goods and may remain on such conveyance for such period as he considers necessary.

(10) POWER TO REQUIRE PRODUCTION OF DOCUMENTS AND ASK QUESTIONS (SECTION 38)

For the purposes of carrying out the provisions of this Act, the proper officer may require the person-in-charge of any conveyance or animal carrying imported goods or export goods to produce any document and to answer any questions and thereupon such person shall produce such documents and answer such questions.

(11) EXPORT GOODS NOT TO BE LOADED ON VESSEL UNTIL ENTRY-OUTWARDS GRANTED (SECTION 39)

The master of a vessel shall not permit the loading of any export goods, other than baggage and mail bags, until an order has been given by the proper officer granting entry-outwards to such vessel.

(12) EXPORT GOODS NOT TO BE LOADED UNLESS DULY PASSED BY PROPER OFFICER (SECTION 40)

The person-in-charge of a conveyance shall not permit the loading at a customs station -

- (a) of export goods, other than baggage and mail bags, unless a shipping bill or bill of export or a bill of transhipment, as the case may be, duly passed by the proper officer, has been handed over to him by the exporter;
- (b) of baggage and mail bags, unless their export has been duly permitted by the proper officer.

(13) DELIVERY OF EXPORT MANIFEST OR EXPORT REPORT (SECTION 41)

The person-in-charge of a conveyance carrying export goods shall, before departure of the conveyance from a customs station, deliver to the proper officer in the case of a vessel or aircraft, an export manifest electronically and in the case of a vehicle, an export report, in the prescribed form.

The export manifest may be presented in manner other than electronically if it is allowed by Commissioner of customs.

The person delivering the export manifest or export report shall at the foot thereof make and subscribe to a declaration as to the truth of its contents.

If the proper officer is satisfied that the export manifest or export report is in any way incorrect or incomplete and that there was no fraudulent intention, he may permit such manifest or report to be amended or supplemented.

(14) NO CONVEYANCE TO LEAVE WITHOUT WRITTEN ORDER (SECTION 42)

The person-in-charge of a conveyance which has brought any imported goods or has loaded any export goods at a customs station shall not cause or permit the conveyance to depart from that customs station until a written order to that effect has been given by the proper officer.

No such order shall be given until -

- (a) the person-in-charge of the conveyance has answered the questions put to him under section 38;
- (b) the provisions of section 41 have been complied with;
- (c) the shipping bills or bills of export, the bills of transhipment, if any, and such other documents as the proper officer may require have been delivered to him;
- (d) all duties leviable on any stores consumed in such conveyance, and all charges and penalties due in respect of such conveyance or from the person-in-charge thereof have been paid or the payment secured by such guarantee or deposit of such amount as the proper officer may direct;
- (e) the person-in-charge of the conveyance has satisfied the proper officer that no penalty is leviable on him under section 116 or the payment of any penalty that may be levied upon him under that section has been secured by such guarantee or deposit of such amount as the proper officer may direct;
- (f) in any case where any export goods have been loaded without payment of export duty or in contravention of any provision of this Act or any other law for the time being in force relating to export of goods, -
 - (i) such goods have been unloaded, or
 - (ii) where the Assistant Commissioner of Customs or Deputy Commissioner of Customs is satisfied that it is not practicable to unload such goods, the person-in-charge of the conveyance has given an undertaking, secured by such guarantee or deposit of such amount as the proper officer may direct, for bringing back the goods to India.

(15) EXEMPTION OF CERTAIN CLASSES OF CONVEYANCES FROM CERTAIN PROVISIONS OF THIS CHAPTER (SECTION 43)

The provisions of sections 30, 41 and 42 shall not apply to a vehicle which carries no goods other than the luggage of its occupants.

The Central Government may, by notification in the Official Gazette, exempt the following classes of conveyances from all or any of the provisions of this Chapter -

- (a) conveyances belonging to the Government or any foreign Government;
- (b) vessels and aircraft which temporarily enter India by reason of any emergency.

II. CLEARANCES OF IMPORTED GOODS AND EXPORT GOODS (SECTION 44 TO 51)

Chapter VII contains the provisions pertaining to clearances of imported or export goods under section 44 to

51. As per Section 44, the provisions of this chapter shall not apply (a) Baggage and (b) Goods imported or to be exported by post.

The following terms need to know before moving to the provisions of clearances:

1. "bill of entry" means a bill of entry referred to in section 46 [Section 2(4)]
2. "bill of export" means a bill of export referred to in section 50 [Section 2(5)]
3. "entry" in relation to goods means an entry made in a bill of entry, shipping bill or bill of export and includes in the case of goods imported or to be exported by post, the entry referred to in section 82 or the entry made under the regulations made under section 84 [Section 2(16)]

ENTRY OF GOODS ON IMPORTATION (SECTION 46)

Under Section 46(1) of the Customs Act, an Importer of any goods, other than goods intended for transit or transhipment is required to file electronically a "Bill of Entry for home consumption" or "for warehousing".

Bill of Entry is required to be presented electronically; however, the commissioner of customs may, in cases where it is not feasible to make entry by presenting electronically allow an entry to be presented in any other manner.

If the Bill of Entry at the time of presentation is not reasonably complete in all material particulars, the proper officer may, pending the production of such information, permit him, previous to the entry thereof

- (a) to examine the goods in the presence of an officer of customs, or
- (b) to deposit the goods in a public warehouse appointed under section 57 without warehousing the same.

Bill of entry shall include all the goods mentioned in bill of lading or other receipt given by the carrier to the consigner. [Section 46(2)]

A bill of entry may be presented at any time after the delivery of the import manifest or import report. However, the Commissioner of Customs may in any special circumstances permit a bill of entry to be presented before the delivery of such report. [Section 46(3)]

Further, a bill of entry may be presented even before the delivery of such manifest if the vessel or the aircraft by which the goods have been shipped for importation into India is expected to arrive within thirty days from the date of such presentation.

The importer while presenting a bill of entry shall at the foot thereof make and subscribe to a declaration as to the truth of the contents of such bill of entry and shall, in support of such declaration, produce to the proper officer the invoice, if any, relating to the imported goods [Section 46(4)].

If the proper officer is satisfied that the interests of revenue are not prejudicially affected and that there was no fraudulent intention, he may permit substitution of a bill of entry for home consumption for a bill of entry for warehousing or vice versa.[Section 46(5)]

BILL OF ENTRY

The Bill of Entry inter alia, has columns for indicating description of goods, value, quantity, marks and numbers, country of origin etc.

Kinds of Bills of Entry

There are three kinds of Bills of Entry viz., (i) Bill of Entry for Home-consumption (White Colour) (ii)

Warehousing (into-Bond) Bill of Entry (Yellow Colour) (iii) Bill of Entry for Clearance 'Ex-Bond' (Green Colour).

Forms of the Bill of Entry

The home-consumption Bill of Entry which is printed on white paper is referred to as "white Bill of Entry", the "into Bond" or "Warehousing Bill of Entry" is printed on yellow paper and "ex-bond" is printed on green paper. Each Bill of Entry has to be filed in quadruplicate. The columns in original are printed in black, in blue in duplicate and in violet in triplicate and in green in quadruplicate.

Circular No. 16/ 2012 Cus dated 13-06-2012 provides for procedure followed for import of Indian vessels and filing of import manifest, Bill of Entry.

Section 29 of the Customs Act, 1962 read with Section 2(22) and 2(25), the term 'imported goods', *inter alia*, includes vessels entering India from any place outside the country (India). These vessels may fall into any of the following category (i) Foreign flag vessels i.e., vessels that have been registered outside India and which carry imported/ exported goods or passengers, during its foreign run (voyage from a port outside India to an Indian port, whether touching any intermediate port in India or not); (ii) Vessel entering India for the first time on arrival in the country, for registration as Indian Flag vessel; (iii) Vessels which are intended for conversion from foreign run to coastal run/ trade (voyage between two or more Indian ports); and (iv) Vessels which are brought into India for breaking up.

Foreign flag vessels: These are the vessels that are registered abroad and its entry into the country is for carrying cargo or passengers, as a conveyance. Hence, there is no requirement for filing an IGM, Bill of Entry for foreign flag vessel which is being used as conveyance. However, the requirement for filing an import manifest in the prescribed manner for the goods or passengers which are being carried in the vessel, on its entry into an Indian port in terms of the provisions under Section 30 of the Customs Act needs to be complied with.

Indian Flag Vessel: In terms of the provisions of Part-V of the Merchant Shipping Act, 1958, vessels entering into India for the first time, are required to be registered with specified authority of the Mercantile Marine Department as Indian ship, which can then display the national character of the ship as Indian Flag Vessel for the purpose of Customs and other purposes specified in the said Act. Such Indian ship or vessel may be used for foreign run or exclusively for coastal run/ trade. Further, any ship or vessel may be taken outside India or chartered for coastal trade in India, only after obtaining the requisite licence from the Director General of Shipping, under the provisions of Section 406 or 407, respectively, of the said Merchant Shipping Act. Hence, in all such cases the Customs declarations such as IGM, Bill of Entry is required to be filed with jurisdictional Customs authority.

Vessels for conversion into coastal run: Any vessel could be used for coastal run/ trade after obtaining requisite clearance from Director General of Shipping and on fulfilment of certain specified conditions under Section 407 of the Merchant Shipping Act, 1958. In case of foreign going vessel, exemption from import duties, including CVD, have been extended vide serial No.462 of notification No.12/2012-Cus. dated 17.03.2012, subject to prescribed conditions, which binds the importer to file fresh Bill of Entry at the time of its conversion for coastal run/ trade and payment of applicable duty on such conversion of vessel for costal run/ trade. Similarly, excise duty is also payable on vessels which are being used for coastal trade vide serial No.306 of notification No.12/2012-Cus. dated 17.03.2012. Hence, if any Indian Flag vessel which is used for time being as foreign going vessel is converted for use in coastal trade or any vessel which is to be used for coastal trade, there is a need to file a Bill of Entry for payment of applicable duty as CVD.

Vessels for breaking up: Vessel and other floating structures intended for breaking up are liable to payment of applicable duty. All vessels for the transport of persons or goods, falling under heading 8901 (excluding those which are imported for breaking up) are fully exempt from payment of import duty under vide serial No.461 of notification No.12/2012-Cus. dated 17.03.2012, subject to the condition that the importer should file fresh Bill of Entry at the time of its breaking up of the vessel after its importation. Hence, in these cases the importer has to file an IGM and Bill of Entry, claiming the exemption as may be applicable, at the time of initial import and later file fresh Bill of Entry at the time of breaking up of the vessel as per the condition attached to the aforesaid exemption.

In view of the above, it is clarified that in respect of foreign flag vessels, for Indian flag vessels, there is no requirement of filing of IGM and Bill of Entry, since its usage is as conveyance. In respect of Indian flag vessels and vessels for breaking up as explained in para 3.3 and 3.5 above, the importer has to file IGM and Bill of Entry, under the provisions of the Customs Act, 1962. As regards the vessel for conversion into costal run/ trade as detailed in para 3.4, since the changes in the duty structure for levy of CVD on vessels which are being converted for coastal trade was initially imposed from 1.3.2011, and subsequently retrospective exemption has been provided for the period 1.3.2011 to 16.3.2011 vide clause 129 of the Finance Act, 2012, the requirement for filing IGM and Bill of Entry may be insisted in all such cases w.e.f. 17.03.2012, that is the date from which levy of CVD has come into force.

It is also clarified that all vessels including foreign going vessels for its entry into / exit from the country during its journey as foreign going vessel and the Indian flag vessel / Indian Ship for subsequent use as foreign going vessel would not require filing of IGM and Bill of Entry as conveyance, since the same are not imported goods to be cleared for home consumption.

Accordingly, the field formations may adjudicate the cases involving any violation where the IGM or Bill of Entry in respect of import of vessel were not filed at the time of import, on its first arrival in India or on its conversion into coastal trade and appropriate penal action be taken against the offenders.

The above instructions may be brought to the notice of all the concerned immediately through appropriate Public Notice.

The following basic documents are to be filed along with the Bill of Entry:

1. *Invoice.*
2. *Indent and acceptance correspondence pertaining to the Imported goods.*
3. *Bill of Lading in respect of sea-consignments/Airway Bill in respect of Air Consignments.*
4. *Letter of credit or Bill of exchange.*
5. *Insurance policy or Insurance certificate.*
6. *Import licence (Customs purpose copy).*
7. *Small Scale Industries Certificate in respect of Imports sought to be covered under Open General Licence (OGL) and Imports subjected to Actual Users (AU) conditions.*
8. *Catalogue, drawing, write up, analysis certificate as the case may be, in respect of the goods sought to be cleared.*
9. Any other connected/relevant document.

Important Notes: Bill of Entry submitted under Section 46 for clearance of imported goods and shipping bill submitted for export of goods require to be filed electronically (Budget 2011).

PROCEDURE OF BILL OF ENTRY UNDER E-FILING [BILL OF ENTRY (ELECTRONIC DECLARATION) REGULATIONS, 2011]

Notification No. 79/2011 – Cus (N.T.), Dated 25.11.2011 prescribes the procedure of bill of entry under E-filing [Bill of Entry (Electronic Declaration Regulations), 2011]

The following terms are defined under this notification as under:

- (a) "authorised person" means an importer or a person authorised by him who has a valid licence under the Customs House Agents Licensing Regulations, 2004;
- (b) "annexure" means annexure to these regulations;
- (c) "bill of entry" means electronic declaration accepted and assigned a unique number by the Indian Customs Electronic Data Interchange System, and includes its print-outs;
- (d) "electronic declaration" means particulars relating to the imported goods that are entered in the Indian Customs Electronic Data Interchange System;
- (e) "ICEGATE" means Indian Customs Electronic Data Interchange Gateway, an e-commerce portal of the Central Board of Excise and Customs;
- (f) "service centre" means the place specified by the Commissioner of Customs where the data entry of an electronic declaration, is carried out;

The authorised person may enter the electronic declaration in the Indian Customs Electronic Data Interchange System by himself through ICEGATE or by way of data entry through the service centre by furnishing the prescribed particulars.

The bill of entry shall be deemed to have been filed and self-assessment of duty completed when, after entry of the electronic declaration in the Indian Customs Electronic Data Interchange System either through ICEGATE or by way of data entry through the service centre, a bill of entry number is generated by the Indian Customs Electronic Data Interchange System for the said declaration.

After the completion of assessment, the authorised person shall present the original bill of entry (customs copy) and duty-paid challan and supporting import documents to the proper officer of customs for making an order permitting clearance, after examination of the imported goods if so required.

After making an order under regulation 5, the proper officer shall generate duplicate bill of entry (importer's copy) and the triplicate bill of entry (exchange control copy).

The original bill of entry (customs copy) along with supporting import documents shall be retained by the proper officer of customs and after suitable endorsements the duplicate bill of entry (importer's copy) and the triplicate bills of entry (exchange control copy) shall be handed over to the authorized person.

RESTRICTIONS ON CUSTODY AND REMOVAL OF IMPORTED GOODS (SECTION 45)

All imported goods unloaded in a customs area shall remain in the custody of such person as may be approved by the Commissioner of Customs until they are cleared for home consumption or are warehoused or are transshipped.

The person having custody of any imported goods in a customs area -

- (a) shall keep a record of such goods and send a copy thereof to the proper officer;
- (b) shall not permit such goods to be removed from the customs area or otherwise dealt with, except

under and in accordance with the permission in writing of the proper officer.

If any imported goods are pilfered after unloading thereof in a customs area while in the custody of a person, that person shall be liable to pay duty on such goods at the rate prevailing on the date of delivery of an import manifest or, as the case may be, an import report to the proper officer under section 30 for the arrival of the conveyance in which the said goods were carried.

CLEARANCE OF GOODS FOR HOME CONSUMPTION (SECTION 47)

Where the proper officer is satisfied that any goods entered for home consumption are not prohibited goods and the importer has paid the import duty, if any, assessed thereon and any charges payable under this Act in respect of the same, the proper officer may make an order permitting clearance of the goods for home consumption.

Where the importer fails to pay the import duty within two days excluding holidays from the date on which the bill of entry is returned to him for payment of duty, he shall pay interest at such rate, not below ten percent and not exceeding thirty six percent per annum, as is for the time being fixed by the Central Government, by notification in the Official Gazette, on such duty till the date of payment of the said duty.

If the Board is satisfied that it is necessary in the public interest so to do, it may, by order for reasons to be recorded, waive the whole or part of any interest payable under this section.

PROCEDURE IN CASE OF GOODS NOT CLEARED, WAREHOUSED, OR TRANSHIPPED WITHIN THIRTY DAYS AFTER UNLOADING (SECTION 48)

If any goods brought into India from a place outside India are not cleared for home consumption or warehoused or transhipped within thirty days from the date of the unloading thereof at a customs station or within such further time as the proper officer may allow or if the title to any imported goods is relinquished, such goods may, after notice to the importer and with the permission of the proper officer be sold by the person having the custody thereof.

However, the time period of 30 days shall not be applicable in the following cases:

- (a) animals, perishable goods and hazardous goods, may, with the permission of the proper officer, be sold at any time;
- (b) arms and ammunition may be sold at such time and place and in such manner as the Central Government may direct.

STORAGE OF IMPORTED GOODS IN WAREHOUSE PENDING CLEARANCE (SECTION 49)

Where in the case of any imported goods, whether dutiable or not, entered for home consumption, the Assistant Commissioner of Customs or Deputy Commissioner of Customs is satisfied on the application of the importer that the goods cannot be cleared within a reasonable time, the goods may, pending clearance, be permitted to be stored for a period not exceeding 30 days in a public warehouse, or in a private warehouse if facilities for deposit in a public warehouse are not available; but such goods shall not be deemed to be warehoused goods for the purposes of this Act, and accordingly the provisions of Chapter IX shall not apply to such goods.

The commissioner may further extend by a period of 30 days at a time.

CLEARANCE OF EXPORT GOODS

While there is very urgent need to promote exports and earn the most needed valuable foreign exchange/it

does not necessarily mean that the export goods can be allowed without restriction and/or, without observing any formalities.

Export should be in accordance with rules and regulations to be implemented "at the point of exit" and the authority which can enforce such rules and regulations is the Customs Department. The following are the provisions pertaining to Exports of goods under Customs Act:

ENTRY OF GOODS FOR EXPORTATION (SECTION 50)

The exporter of any goods shall make entry thereof by presenting electronically to the proper officer in the case of goods to be exported in a vessel or aircraft, a shipping bill, and in the case of goods to be exported by land, a bill of export in the prescribed form.

However, the Commissioner of Customs may, in cases where it is not feasible to make entry by presenting electronically, allow an entry to be presented in any other manner.

The exporter of any goods, while presenting a shipping bill or bill of export, shall make and subscribe to a declaration as to the truth of its contents.

- (i) The Customs allow imports/exports only through authorised places along the coast/across the land frontier and by air. For this purpose "customs ports", "customs Airports", "land customs stations" are notified by the Central Govt. under Section 7(a), (b) and (c) Customs Act, 1962.
- (ii) The master of the vessel should not permit loading of the cargo before 'Entry Outwards' is granted by the Customs Department and export cargos can be taken on board the vessel or aircraft or a vehicle (for the land route), only under cover of a duly passed Shipping Bill/Bill of export with the permission of the proper (Customs) officer - (vide Sections 39 and 40 of the Customs Act, 1962).
- (iii) In terms of Section 50 of the Customs Act, 1962 a shipping Bill or Bill of Export (in respect of exports through land route) is to be filed by the exporter or his authorised agent, in the prescribed form [prescribed under Shipping Bill and Bill of Export (Form) Regulations 1976 made under Section 157 of the Customs Act, 1962]
- (iv) The Shipping Bill so filed should be assessed. The term "assessment" as defined under Section 2(2) of the Customs Act includes assessment to 'nil' duty also. Under Section 18 of the Customs Act, 1962 provisional assessment to duty of goods meant for export is possible under the circumstances indicated in that section. Thereafter the goods shall be examined physically and permitted shipment by means of passing on the shipping bill a 'Let Export' or 'Let Ship' order.
- (v) The 'assessable value' for export as declared in the shipping bill should be in accordance with the provisions of Section 14 of the Customs Act, 1962. (Declared value is subject to verification as to its correctness or otherwise by Customs authorities).
- (vi) For assessing the goods for export to duty and granting an order of 'Let Export' under Section 51 of the Customs Act, the export goods, should not be "prohibited goods" - prohibited for export under the Customs law or prohibited for export under any other law for the time being in force - The Customs Department in pursuance of Section 11(2)(u) of the Customs Act, 1962 is also empowered to prevent the contravention of any other law noticed in the course of export.
- (vii) Power to confiscate the export goods, "attempted to be improperly exported" etc. has been endowed on the Customs Department under Section 113(a) to (l) of the Customs Act, 1962.
- (viii) Under Section 114 of the Customs Act, "penalty for attempt to export goods improperly", on persons concerned could be imposed (in addition to confiscation of the goods), not exceeding five times the

value of the goods.

- (ix) It is also provided in Section 127 of the Customs Act, that award of confiscation and penalty by Customs shall not prevent infliction of any punishment by way of prosecution (in deserving deliberate and grave offences) under Section 132 and 135 read with Section 137 of the Customs Act, 1962.

CLEARANCE OF GOODS FOR EXPORTATION (SECTION 51)

Where the proper officer is satisfied that any goods entered for export are not prohibited goods and the exporter has paid the duty, if any, assessed thereon and any charges payable under this Act in respect of the same, the proper officer may make an order permitting clearance and loading of the goods for exportation.

DOCUMENTATION FOR EXPORT

For effecting shipments, the exporter or his agents should file a shipping bill electronically (Section 50 of the Customs Act), (the quadruplicate copy is filed for purposes of Export promotion). These shipping bills could be filed in the Custom House or Air Cargo Complex, 14 days before the arrival of the loading vessel/aircraft. However, the commissioner of customs may, in cases where it is not feasible to make entry by presenting electronically, allow an entry to be presented in any other manner. Steamer agents normally file applications in the custom House in advance of 'grant of Entry outwards' of the vessel. In the application they furnish, the particulars of the vessel viz. Name, Nationality, Tonnage, the port for which the vessel will load cargo, the nature of cargo, etc. Immediately on presentation of the application, a number called 'Rotation No.' (Export Manifest No. or Export General Manifest No.) is assigned. After the compliances of the above requirements the exporters or their agents may present the shipping bills for the export of their goods. Subsequently, after arrival of the vessel and when she is about to start loading export cargo, orders for 'Entry Outwards' are given by the Customs Authorities. In terms of Section 39 of the Customs Act, the person in charge of the vessel should not allow loading of cargo before the grant of Entry outwards. The facility afforded to the intending Exporters to file shipping bills immediately after the filing of "Application for Entry outwards" by steamer agents, which is normally done 14 days ahead of the arrival of the vessel, is to enable the exporters to complete all the customs formalities and keep the goods ready for loading.

(a) Documents to be filed along with the Shipping Bill

1. G.R.(Guarantee Remittance)/SDF (Statutory declaration Form, used in e-filing) form in duplicate in respect of exports to all countries except Afghanistan and Pakistan.

Note: To Pakistan and Afghanistan - EP forms in triplicate are to be prepared in lieu of GR forms and are to be filed along with the shipping bill, with the approval of the Reserve Bank of India.

2. Four copies of Export Invoices/ indicating all particulars such as, the number of packages, quantity, unit price, full description of the goods value in total, CIF; FOB or C&F, as the case may be.

3. Packing List.

4. Export Contract; Letter of Credit and all connected correspondence.

5. Inspection/Examination certificates from Agmark grading authorities in respect of agricultural commodities.

6. Pre-shipment and compulsory quality control certificates in respect of goods covered under the compulsory quality control and preshipment inspection scheme (under the Export (Quality Control and Inspection) Act, 1963).

7. ARE-1 or ARE-2 as applicable under Rules 18 or 19, Central Excise Rules, 2002 Forms (Application for

Removal of Excisable Goods for Export) in duplicate duly completed in all respects for the export of excisable goods.

8. In regard to 'handicraft exports' items which fall under the category "India items" e.g.. wall hangings/woolen carpets/mirror or bidriware/ etc. should be covered by a certificate issued by All India Handicrafts Board.

9. Garments and Textile for their export, should be validly covered by an "Inspection Certificate" from the Textile Committee. In addition, for export to USA "visas" should also be endorsed by the Textile Committee in the format "Special Customs Invoice".

In addition, the exporter should make and subscribe to a declaration at the bottom of the copies of shipping Bills as to the truth of the contents, in terms of Section 50(2) of the Customs Act, 1962 and other laws.

(b) Kinds of Shipping Bill

There are four categories of shipping bills viz. those

- (i) for Free goods;
- (ii) for Dutiable goods, assessable to duty and/or cess;
- (iii) for shipment under claim for drawback (Green Shipping bill); and
- (iv) for shipment from bond i.e., 'Ex-bond'.

Notification No. 80/2011- Cus (N.T.), Dated 25.11.2011 prescribes the **Shipping Bill (Electronic Declaration) Regulations, 2011**.

These Regulations shall apply to export of goods from all customs stations where the Indian Customs Electronic Data Interchange System is in operation.

The Following terms are defined under this regulation as under:

- (a) "authorised person" means an exporter or a person holding a valid licence under the Custom House Agents Licensing Regulations, 2004 and authorised by such exporter;
- (b) "annexure" means annexure to these regulations;
- (c) "electronic declaration" means particulars relating to the export goods entered in the Indian Customs Electronic Data Interchange System;
- (d) "ICEGATE" means Indian Customs Electronic Data Interchange Gateway, an e-commerce portal of the Central Board of Excise and Customs;
- (e) "service centre" means the place specified by the Commissioner of Customs where the data entry for an electronic declaration, is carried out;
- (f) "shipping bill " means an electronic declaration accepted and assigned a unique number by the Indian Customs Electronic Data Interchange System, and includes its print-outs;

The authorised person may enter the electronic declaration in the Indian Customs Electronic Data Interchange System by himself through ICEGATE or by way of data entry through the service centre by furnishing the prescribed particulars.

The shipping bill shall be deemed to have been filed and where applicable self assessment of duty completed when, after entry of the electronic declaration in the Indian Customs Electronic Data Interchange System either through ICEGATE or by way of data entry through the service centre, a number is generated

by the Indian Customs Electronic Data Interchange System for the said declaration.

The checklist together with the supporting export documents and challan evidencing payment of duty and/or cess, if any, shall be presented to the proper officer of customs for making an order permitting clearance, for loading of goods for exportation, after examination of the export goods if so required.

After making an order, the proper officer shall generate the original (customs copy), exporter's copy, exchange control copy and the export promotion copy of shipping bills.

The original (customs copy) of the shipping bill and the checklist shall be retained by the proper officer. The exporter's copy exchange control copy and the export promotion copy of shipping bill shall after suitable endorsements be handed over to the authorised person. Transference copies of shipping bill shall be generated wherever necessary.

EXPORT GOODS AND TARIFF SCHEDULE

The goods are properly classified for collection of export duty (under Second Schedule to Customs Tariff Act, 1985 – Export Tariff) and Cess (under Cess schedule) as the case may be, by indicating the rates there against. The Export Tariff is a selective Tariff and contains only 49 items. Articles not covered by any of these 49 items are not leviable to Export duty. Even in respect of these 49 items, the effective rate of duty has to be determined with reference to 'exemption notifications' issued under Section 25 of the Customs Act. Thus, very few items are actually liable to duty on export. The purpose/intention of the Government in having a "selective tariff" on the Export side is not to burden the Export goods with "duty" which would/may render them, not competitive, to whatever little extent, in foreign markets. Export duty is, therefore, levied and collected mostly on items in respect of which India enjoys a sellers market.

Commodities, as enumerated in the Cess Schedule, which forms part of the Customs Tariff (Working Schedule) attract cesses under various enactments (as detailed thereunder). Most of the commodities mentioned in the cess schedule require levy of cess at 1/2% ad-valorem (in addition to Export duty wherever export duty in respect of the commodity is leviable). In respect of some of the commodities "tariff values" are fixed by the Ministry (as indicated in the cess schedule) with effect from the first July of every year. In such cases/ the cess is calculated on the "tariff value" irrespective of the "invoice value".

The assessable value of Export goods leviable to *ad valorem* duties (other than tariff valued items) is always the FAS (Free Alongside) values. In the shipping Bill this is indicated as "Real Value" also. This is derived from the contract value or the price contracted upon for export, between the Indian Exporter and the Foreign buyer. If the contracted price is anything other than FAS, then the value for customs purposes-FAS (the price for delivery at the place of Exportation - Section 14 of the Customs Act, 1962) is arrived at and duty is calculated on the FAS value so arrived at.

SHIPMENT (EXPORT) UNDER CLAIM FOR DRAWBACK

The term 'drawback' is applied to certain amount of duties of customs, sometimes the whole, sometimes only a part, paid back by Government on the exportation of commodities on which they were levied. To entitle goods to drawback, they must be exported to a foreign port, the object of the relief afforded by the drawback being to enable the goods to be disposed of in the foreign market as if they have never been taxed at all.

For Customs purposes "drawback" means the refund of custom duty, service tax and the Central Excise duty that are chargeable/charged on imported and indigenous materials and services used in the manufacture of goods exported.

From the point of view of "Export Promotion" it is a relief of duty given to exporters, both manufacturer and

merchant exporters.

There are two categories of materials which are used in the manufacture of goods exported, namely imported and indigenous. Consequently, drawback is to be paid in respect of three types of taxes: Import duty, service tax and Excise duty.

The provisions relating to drawback are enumerated in Chapter X, Sections 74 to 76 of the Customs Act, 1962. Of these, Section 75 deals with the payment of "drawback on Imported materials used in the manufacture of goods which are exported".

Under Section 75(2) of the Customs Act, 1962, the Central Government is empowered to make rules for payment of drawback and such rules provide:

- (a) for the payment of drawback equal to the amount of duty paid on the Imported materials used in the manufacture of goods or as is specified in the rules as the average amount of duty paid on the materials of that class or description of goods either by manufacturers generally or by any particular manufacturer.
- (b) for the production of such certificates documents and other evidence in support of each claim of drawback, as may be necessary etc.

The rules made in this regard, read with Section 37 of the Central Excise Act, 1944 are called "The Customs and Central Excise Duties Drawback Rules, 1995.

CLAIM FOR DRAWBACK — EXPORTERS DECLARATIONS AND DOCUMENTS

In terms of the above said rules at the time of export of the goods the exporter inter alia shall:

- (i) File a Shipping Bill "under claim for Drawback". (Green Shipping Bill)
- (ii) State in the above said Shipping Bill, the description quantity and such other particulars as are necessary for deciding whether the goods are entitled to drawback and if so at what rate or rates.
- (iii) File the documents as enumerated already and the Customs formalities to be completed for shipment are the same as detailed above in respect of goods shipped under claim for drawback also under cover of a "Green Shipping Bill".

On completion of shipments the drawback claimed on exports is scrutinised in the drawback department or the drawback unit of the Custom House or Air Cargo Complex and payments are made by cheques drawn in favour of banks as nominated by Exporters.

PROCEDURE FOR EXPORTS THROUGH INLAND CONTAINER DEPOTS

(i) Introduction

Shipping is the cheapest way to transport goods. The cost per mile of water borne cargo is half the cost of any other form of long distance transport. Cargo comes in all shapes and sizes.

Each item of cargo must be individually arranged, counted, handled and put on board the ship according to a detailed cargo plan. This involves time and man-power and is costly. Therefore, it is quicker and cheaper to have cargo of a standard shape and size which is easy to handle and stack. Such a cargo type is termed a "Unit load" which in transportation usually means a "container".

(ii) Evolution

In response to "Cost cutting" and "time saving" requirements of modern trade "containerisation" has come

about in the past decade. This system was introduced in "sea transport" in 1949 when John Wollan sent a "box" of sports goods across Irish sea. The "white pass and Yukon route" introduced deep sea container traffic from Canada and the world's first fully integrated container service came into being in 1955. The world's largest container shipping service was founded in USA-Malcolm Mc Clean Service.

A modified version of 'containerisation arose in 1968. It is known as "Lighter" aboard ship"- FLASH. In the flash system, lighters are loaded on the shore and floated out to the ship waiting off-shore. The ship lands the lighters on board with its own crane (Gantry crane) and stacks them there high like containers. At the port of arrival the lighters are unloaded and floated to shore. This saved/saves both port costs and cuts time spent waiting for an empty berth.

(iii) Conventional cargo ships vis-a-vis container ships

Conventional cargo ships are not being swept away from the seas by containerisation. Only on certain busy routes as the North Atlantic run/ has the switch over to containers been near complete. Elsewhere, the conventional cargo, ship has maintained its hold. For a small port handling a few thousand tonnes of cargo, it does not make economic sense to instal a container berths handling equipment and road and rail connections. Conventional cargo ships are helped by the fact that not all cargoes will economically containerise. Such cargoes are usually large (logs for instance) or heavy (steel plates). Another requirement in respect of containers is that for "every box" at sea another three are needed on land; one at the port of departure, one at the port of arrival and one being repaired.

(iv) What is a Container?

A container is simply a box. It is no more complex than a truck body, a railway freight van or a ship's hold. Containers are made of aluminium, steel, fibre glass or plywood for lightness with steel frames to give strength. Standard sizes for containers are 40, 20, or 10 feet long, 8ft. wide and 8ft. in height. Some have open tops or sides for loading special cargo. Liquids are carried in boiler shaped tanks surrounded by rectangular frame work. Other containers are insulated or refrigerated and are constructed according to International standards and inspected by Insurance companies.

(v) How are they loaded on the ship

Container ships are built in vertical cells. The container slips into position in each cell down guide rails. The containers sit on the top of each other in the ship's hold. Container ships towards insuring loss over board, are designed with distinctive concave low shapes to keep waves clear of the decks.

(vi) Handling of containerised cargo in India

In India, procedures have been drawn up for handling containerised cargo both on the Import and Export side. The Import and Export Cargo containerisation presupposes formation of Inland Container Depots and should have the necessary arrangement and infrastructure of rail and road connections.

Inland Container Depots can be opened or can come up only in places which are appointed places for unloading of Imported goods and the loading of Export goods or any class of such goods by Central Government, by notification in the official gazette as contemplated under Section 7 of the Customs Act, 1962. In the Southern Region, Bangalore, Coimbatore and Anaparte (near Guntur) have been declared as I.C.Ds.

(vii) Categories of Containerised Cargo

Containerised Cargo is divided into two categories viz. Full Container Load (FCL) and Loose Container Load

(LCL). By FCL, it is understood that the entire cargo in a particular container belongs to a single consignee of a particular port, place, while LCL denotes container containing several consignments (Break Bulk) belonging to various consignees of a particular port/place.

(viii) Short shipment Notice

In the event of the Export goods passed for shipment, not shipped (shut out) or short shipped, Short Export Rules, 1963, framed in exercise of powers conferred on the Central Government, under Section 156 Customs Act, 1962, require information of short shipment non-shipment (shut out) to be given to the customs department before the expiration of 7 days from the date of the departure of the vessel. Failure to comply with this provision entails penalty not exceeding `100/-.

No particular form for intimating short shipment or non-shipment (shut out) of goods has been "prescribed" as "form of Notice" under Short Export Rules. But for the convenience, the trade has been notified to file such notices in Triplicate with the required particulars in Annexures 'A' and 'B' to this study.

On receipt of Short-shipment/non-shipment (shut out) notices, the Customs Department returns one copy to the Exporters or to their agents duly acknowledging the receipt of the notice; sends one copy to Reserve Bank of India who are policing the repatriation of Export sale proceeds from abroad, as declared on the GR form and the third copy is connected to the relative Shipping Bill in the Export Manifest of the vessel filed by the Steamer agents. One Short shipment/non-shipment notice is required to be filed for each Shipping Bill. Failure to comply with the above requirement, apart from causing inconvenience to the Exporters, in explaining the short realisation of the export sale proceeds to the Reserve Bank of India, at the appropriate time, will render the Exporters and/or their agents liable for penal action under Rule (3) of the Short Export Rules, 1963.

(ix) Amendment application in lieu of Short Shipment Notices

In the event, the goods covered by a Shipping Bill have been "shut out" in full, the Shippers/Exporters are allowed to amend the ship's/vessel's name on the shipping bill, when the new ship had "entered outwards" in the port, and ship the goods. This can be done provided the period allowed under the notice of Short Export Rules, 1963 (viz. 7 days) had not lapsed.

PROCEDURE FOR EXPORTS OF CONTAINERISED CARGO FROM INLAND CONTAINER DEPOTS

The exporters file shipping bills at the I.C.D. The Shipping Bills will be filed in five copies, original, duplicate, triplicate and two transference copies which are in distinct colors for easy identification and handling. The documents that are to be filed along with the shipping bills are as detailed earlier. In addition to the usual information given on the shipping bills the exporters should mention the Port of Exit and the serial number of the containers. Each container will have different marks and numbers.

Classification and assessment will also be completed at the I.C.D, following usual prescribed checks and formalities as detailed already. The original shipping bill will be retained and the other copies handed over to the exporters for completion of examination and other formalities.

The exporters will submit alongwith the shipping bills the set of G.R. forms (original/duplicate). The "Full Export Value" will be verified as usual on the G.R. Form; original copy of G.R. will be detached at the I.C.D. and will be sent direct to the Reserve Bank of India. The duplicate copy of the G.R. form will be handed over to the exporter alongwith the shipping bills.

The export goods, will be presented to the 'Customs Officer in the "I.C.D. alongwith the Shipping Bills". The

examination will be conducted in accordance with the procedure prescribed for examination of export goods after which the goods will be allowed to be "stuffed" into the containers under Customs supervision. The quantity of goods loaded (number of packages etc. shut out) will be recorded on the shipping bill. Once the goods are loaded into the container, the containers will be sealed with "one time lock" containing identification details as supplied by the Railway and record maintained for the same with the I.C.Ds. Simultaneously, with the stuffing of the goods inside the containers, the exporters will prepare in quadruplicate, the invoices and container-wise packing weight specifications indicating inter alia the number of packages (with marks and numbers, if any), description and total quantity, net weight/packed in each container along with the corresponding shipping bill number. The Customs officers will certify these details on the invoice/packing list. Duplicate copy of the shipping bill will be retained in the I.C.D. and triplicate handed over to the exporter.

The two transference copies of the Shipping bills will be placed in a sealed envelope and handed over to the carriers (Railways) who will be responsible for its being carried alongwith the container and its production to the Customs officer at the port of exit.

At the exit Ports the containers will be allowed to be exported under customs (preventive) supervision on checking of the seals without any further examination (examination will only be done if the seals of the containers are found to have been tampered with or on the basis of any information, doubts etc.) The Preventive officer who will be supervising the loading of the containers will suitably endorse the two transference copies of the shipping bills regarding the fact of shipment.

At the Port of Exit, the Steamer Agents will also file the export manifesto in duplicate regarding the containerised cargo in the 'container cell' to the Preventive Department of the respective Custom House. After shipment of the goods, one transference copy of the shipping bill will be returned to the respective I.C.D.

The Export Manifest transference copies of the shipping Bill and the weekly statement received from the Custom House (Exit ports) will be correlated for finalisation of drawback claims/ Closure of export manifest, etc. at the ICD.

III. GOODS IN TRANSIT (SECTION 52 TO 56)

A conveyance / vessel may reach a port but may not unload the goods at that port. It may halt at the port for any other purpose such as repairs, replenishment of supplies, refueling etc. Once the purpose is over, it may start sailing to the destination port. In this case two ports are involved. Halting port (known as transit port) intermediate port and destination port (called as port of clearance). Such a phenomenon of temporary stay at a port other than a destination port is called transit goods. In transit goods same vessel reaches the port of clearance.

In transshipment, the vessel reaching an intermediate port, transfers the goods to another vessel and the second vessel into which the goods are transferred (loaded) from the 1st vessel, carries the goods to the destination port.

Example: a ship A comes to Mumbai from South Africa and some goods are transshipped (transferred) to some other ship B and the goods are meant to be delivered at Cochin port (destination port) A goes back to South Africa after delivery at Mumbai port and the B reaches Cochin, transshipment took place at Mumbai port.

In brief, in case of transit goods, same vessel reaches the port of clearance after some halt at an intermediate port, but in transshipment some other vessel carries the goods to the destination port. Thus, in

transshipment, at least two vessels are involved. And in the case of both transit and transshipment, the destination port may be Indian Port or Foreign port but the transit/transshipment port is necessarily Indian.

Customs Act, 1962 contains separate provisions for goods in transit in Chapter VIII of the Act. This Chapter consists of Sections 52 to 56. Section 52 of the Act makes it very clear that the provisions of Chapter VIII do not apply to:

- (a) baggage;
- (b) goods imported by post;
- (c) stores.

Sections 53, 54 and 55 have been amended by the Finance (No. 2) Act, 1998, so as to also allow for the transit and transhipment of goods in the following circumstances:

- (a) where goods have arrived in India at a land customs station and are intended to be transhipped to another land customs station or to a port or airport outside India;
- (b) where goods have been carried in a conveyance other than a vessel or aircraft; and
- (c) where goods that have arrived at the port or airport on a vessel or aircraft are required to be transhipped to a land customs station.

The details of the provisions of the Chapter are discussed herein below:

TRANSIT OF CERTAIN GOODS WITHOUT PAYMENT OF DUTY (SECTION 53)

Section 53 of the Act deals with this. Accordingly, any goods imported in a conveyance and mentioned in the import manifest or the import report, as the case may be, as for transit in the conveyance to any place outside India or any Customs station may be allowed to be so transited without payment of duty. The provisions of Section 53 are subject to the provisions of Section 11. It should be noted that Section 53 talks about transit of goods in the same conveyance and not transhipment of goods from one conveyance to another. (Section 54 deals with transhipment of goods imported into India, from one land customs station to another land customs station or to a port or airport outside India).

TRANSHIPMENT OF CERTAIN GOODS WITHOUT PAYMENT OF DUTY (SECTION 54)

Section 54 of the Act provides that where any goods imported into a Customs station are intended for transhipment, a bill of transhipment shall be presented to the proper officer in the prescribed form. But where the goods are being transhipped under an international treaty or bilateral agreement between the Government of India and Government of a foreign country, a declaration for transhipment instead of a bill of transhipment shall be presented to the proper officer in the prescribed form.

Section 54(2) provides that where any goods imported into a Customs station are mentioned in the Import Manifest or import report as the case may be, as for transhipment to any place outside India, such goods may be allowed to be so transhipped without payment of duty. The provisions of Sub-section (2) of Section 54 are subject to the provisions of Section 11.

Sub-section (3) of Section 54 provides that where any goods imported into a Customs station are mentioned in the Import Manifest or import report, as the case may be, as for transhipment:

- (a) to any major port as defined in the Indian Ports Act, 1908 or the Customs Airport at Mumbai, Calcutta, Delhi or Chennai or any other Customs port or Customs airport which the Board may, by

Notification in the Official Gazette, specify in this behalf, or

- (b) to any other Customs station and the proper officer is satisfied that the goods are bona fide intended for transhipment to such Customs station,

the proper officer may allow the goods to be transhipped without payment of duty subject to such conditions as may be prescribed for the due arrival of such goods at the Customs station to which transhipment is allowed.

LIABILITY OF DUTY ON GOODS TRANSITED UNDER SECTION 53 OR TRANSHIPPED UNDER SECTION 54 (SECTION 55)

Under Section 55 of the Act, where any goods are allowed to be transited or transhipped under Sections 53 and 54 respectively, to any Customs station, they shall, on their arrival at such station, be liable to duty and shall be entered in like manner as goods are entered on the first importation thereof and the provisions of this Act and any rules shall so far as may be, apply in relation to such goods.

TRANSPORT OF CERTAIN CLASSES OF GOODS SUBJECT TO PRESCRIBED CONDITIONS (SECTION 56)

Sometimes imported goods may be transported from one part of the country to another part of the country through a foreign territory because of geographical and other constraints. Under the circumstances, Section 56 provides that imported goods may be transported without payment of duty through any foreign territory subject to the Transportation of Goods (Through Foreign Territory) Regulations, 1965. These regulations contemplate the following procedure. Regulations 3 and 10 of these Regulations are extracted herein below:

1. *Consignor to deliver a Bill:*

- (a) Whenever any goods to which these regulations apply are to be transported, the consignor of the goods shall make entry to that effect by presenting to the proper officer a bill (in duplicate) in the form specified in Appendix C to these Regulations.
- (b) Every such consignor shall, while presenting the bill, make and subscribe to a declaration at the foot thereof as to the truth of its contents.

2. *Permission to load goods, etc.:* No person-in-charge of a vessel shall permit the loading of such goods on a conveyance unless:

- (a) the bill relating to them after approval by, and
- (b) a written permission to load the goods from, proper officer are received by him.

3. *Execution of Bond:* Before any such goods are permitted to be loaded on the conveyance, the consignor or the person-in-charge of the vessel shall be required to execute a bond in such form and with such surety or sufficient security as the proper officer may demand, binding himself in an amount not exceeding the value of the goods.

4. *Duties of the person-in-charge of the conveyance:*

- (1) On receipt of the documents referred to in regulation 4, the person-in-charge of the conveyance shall prepare as many sets of Manifest (in triplicate) in the Form specified in Appendix B to these regulations in respect of such goods as there are customs stations to be passed through on the route.

He shall, immediately, on arrival at an customs station of delivery or re-entry, deliver a set of the

manifest along with the bill or bills relating to the goods to the proper officer at the customs station.

- (2) The proper officer shall, after making the necessary checks, make an endorsement on the manifest, retain one copy of the manifest and return the other two copies to the person-in-charge of the conveyance.
 - (3) The person-in-charge of the conveyance shall retain one of the two copies for carrier's record and present the other to the proper officer at the loading station.
 - (4) The person-in-charge of the conveyance carrying such goods shall not leave the customs station until a written permission has been given by the proper officer after checking the manifest presented to him under the regulation.
5. **Delivery of bills at the destination station:** The person-in-charge of the conveyance shall carry with him on the journey all the bills relating to the goods delivered to him and shall immediately on arrival at any customs station deliver to the proper officer such of the bills as relate to the goods unloaded at that station.
6. **Clearance of goods:** Such goods, after being unloaded at any customs station, shall not be cleared unless the proper officer gives a written permission that all the goods so unloaded are entered in the bill or bills delivered to him under these Regulations.
7. **Terms of the bond:** The condition of the bond to be executed under Regulation 5 shall be that if the person-in-charge of the conveyance or the consignor produces proof within a time stipulated in the bond or such extended time as the proper officer may permit that the goods have been produced before the proper officer at destination the bond shall be void; and if such proof be not furnished the executor of the instrument shall be liable to pay an amount equal to the export duty leviable on the goods and such penalty as may be adjudged or imposed by the proper officer under the Customs Act, 1962, the Imports and Exports (Control) Act, 1947 (18 of 1947) or the Foreign Exchange Management Act, 1999 and shall also be liable to forfeit the whole amount of the bond.
8. **Execution of general bond:** Notwithstanding anything contained in these Regulations, the proper officer may permit the person-in-charge of the conveyance or the consignor of goods to enter into a general bond in such form and with such surety or security as the proper officer may deem fit, in respect of transport of goods as above said to be effected from time to time".

DISTINCTIONS BETWEEN TRANSIT AND TRANSHIPMENT GOODS

TRANSIT GOODS	TRANSHIPMENT OF GOODS
1. Goods are <i>lying</i> in the ship at an intermediate port.	Goods are <i>transferred</i> at the intermediate port.
2. Only import manifest has to be submitted for entry.	Bill of transshipment/ declaration is also required for transshipment.
3. Transit is allowed in every port normally.	Transshipment is allowed in specified ports only.
4. No supervision is required for transit goods.	Transshipment takes place under the supervision of the proper officer.
5. No additional conditions or formalities are required.	Specific conditions are imposed if the goods are deliverable at Indian port.
6. Only one conveyance is involved in transit of goods and the same carries the goods to the port of clearance.	At least two conveyances are involved in transshipment and the transferee ship reaches the destination port.

SELF TEST QUESTION

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. Which main documents are required to be prepared for effecting Export of Goods?
2. What is Import manifest? Give the details of its contents.
3. What is a 'Shipping Bill'? How it is prepared and used?
4. What are the kinds of Shipping Bills?
5. What is 'GR' form and how it is obtained?
6. What is the procedure with regard to obtaining of 'Export Trade Licence'?
7. What are the provisions regarding 'Draw back' of duties on Exported goods under Customs Act, 1962?
8. Explain the concept of 'Containerisation' in Import-Export trade and how does it compare with the conventional ships ?
9. How the various customs ports, airports and places are fixed for the purpose of loading/unloading of goods subject to levy of duties of Customs ?
10. Which organisations are involved in clearance of import Cargo ?
11. What is 'Bill of Entry' ? What are the different kinds of 'Bill of Entry' ?
12. What is the procedure of preparation and filing of 'Bill of Entry' ?
13. How are the goods Imported but not cleared by Customs dealt with?
14. What are the provisions in the Customs Act, 1962 with regard to examination of goods before order of clearance?
15. What is "Out of Customs charge" order for delivery of goods?
16. What specific points one should keep in mind in the clearance of imported cargo for home consumption?
17. When are the goods said to be in transit within the meaning of Customs Act, 1962?
18. Distinguish between transit and transshipment of goods.
19. How are the goods in transit treated for the purpose of levying of duties of customs.
20. When does the officer of Customs may permit the transhipment of goods without payment of duty?

SUGGESTED READINGS

- (1) Customs Manual — *Taxmann*
- (2) Customs Law Manual — *R.K. Jain*
- (3) Customs Tariff — *R.K. Jain*
- (4) Indirect Taxes Law and Practice — *V.S. Datey*

CUSTOMS LAW

PART IV: WAREHOUSING, DUTY DRAWBACK, BAGGAGE AND MISCELLANEOUS PROVISIONS

After completion of this part students will be familiar with

- Warehousing provisions
- What are the conditions to be satisfied for warehousing of goods
- The duty drawback provisions
- Baggage provisions and rules thereon
- Provisions pertaining to postal goods
- Goods imported or exported by post and store
- Provisions relating to coastal goods and vessels carrying coastal goods

This part is divided into six sub parts:

- I. Warehousing (Section 57 to 73)
- II. Drawback
- III. Baggage (Section 77 to 81)
- IV. Goods imported or export by Post (Section 82 to 84)
- V. Stores (Section 85 to 90)
- VI. Provisions relating to Coastal goods and Vessels carrying coastal goods (Section 91 to 99)

I. WAREHOUSING (SECTION 57 TO 73)

Goods imported from abroad may be cleared straightaway by the Importers by filing the Customs Clearance document, the Bill of Entry for Home Consumption (White Bill of Entry) along with all the documents, such as Invoice, Purchase Contract, Import Licence (Wherever necessary) and all connected and relevant documents. The above requirements for clearance are stipulated in Section 46 of the Customs Act, 1962.

Section 46 of the Customs Act, 1962 provides that importer shall file a Bill of Entry, either for Home consumption or for Warehousing, in the “prescribed form”. Therefore, the importers who do not intend clearing the imported goods for “Home consumption” may choose to “warehouse” the goods (store the goods under Customs control/custody) and clear the same subsequently either wholly or in part, in piecemeal, on payment of Customs duty.

Warehousing is a very useful facility in export import business. Importer can deposit the dutiable goods in a bonded warehouse without payment of duty. This facility is available to traders as well as importers.

Warehousing facility is availed for the following reasons:

- (i) *The importer may not require the goods immediately.*
- (ii) *He may intend to clear the goods under advance authorisation scheme without payment of import duty if authorization is not on hand at the time of import then he can deposit first and submit the authorization at the time of clearance.*

- (iii) *The importer may not have enough funds to make payment of duty immediately.*
- (iv) *He intends to re-export the imported goods after some process/ repacking, repairing etc.*
- (v) *He wants to avoid heavy demurrage charges imposed by the port.*
- (vi) *Any other reason the importer feels it convenient.*

The prescribed form referred to in Section 46 of the Customs Act 1962 also includes the Bill of Entry for warehousing. This form is also referred to and understood by the following names:

- (a) "Into Bond" Bill of Entry;
- (b) "Yellow" Bill of Entry;
- (c) "Warehousing" Bill of Entry; and
- (d) "Buff" Bill of Entry.

The term "warehouse" for the purposes of the application of the provisions of the Customs Act, 1962 has been defined under Section 2(43) of the Act, as under:

"Warehouse" means a Public (Bonded) warehouse appointed under Section 57 of the Customs Act or a private (Bonded) warehouse "Licensed" under Section 58 of Customs Act, 1962.

Warehouses either "public" or "private", could be "appointed" or "licensed" as above said, only at the places declared by the Central Board of Excise and Customs to be "warehousing stations" by means of notifications in the official gazette. Therefore, warehouses cannot be "appointed" or "licensed" in all places. [Section 9 of the Customs Act, 1962].

In earlier years, the port towns adjacent to the major ports and contiguous areas thereto, which were easily accessible and which could be kept under control of the respective Customs "Warehouse" only was declared as "warehousing stations". For the purpose of convenience, entire cities, talukas, in such cases were generally declared as warehousing stations, generally or for specific purposes.

Consequent upon the increased requirements for adequate warehousing facility, of the trade and industry, now the Government of India's policy in respect of Public (Bonded) warehousing, is to declare selected places, in the areas other than port areas, namely in Inland/Interior areas, as "warehousing stations" under Section 9 of the Customs Act, 1962.

The object behind "appointment of Public (Bonded) warehouses and licensing of Private (Bonded) warehouses" is to afford a facility to the Importers to deposit the imported goods for the specified period, before they are cleared for home consumption or re-export.

Chapter IX (Sections 57 to 73) deals with various provisions relating to warehousing of import goods.
These provisions may be broadly divided into the following headings:

1. *Appointment of public warehouses (Section 57).*
2. *Licensing of Private warehouses (Section 58).*
3. *Warehousing bond (Section 59).*
4. *Permission for deposit of goods in a warehouse (Section 60).*
5. *Period for which goods may remain warehoused (Section 61).*
6. *Control over warehoused goods (Section 62).*

7. *Payment of rent and warehouse charges (Section 63).*
8. *Owner's right to deal with warehoused goods (Section 64).*
9. *Manufacture and other operations in relation to goods in a warehouse (Section 65).*
10. *Power to exempt imported materials used in the manufacture of goods in warehouse (Section 66).*
11. *Removal of goods from one warehouse to another (Section 67).*
12. *Clearance of warehoused goods for home consumption (Section 68).*
13. *Clearance of warehoused goods for exportation (Section 69).*
14. *Allowance in case of volatile goods (Section 70).*
15. *Procedure for taking out/removal of goods from warehouse (Sections 71 and 72).*

The above provisions, as amended, are explained as under:

1. APPOINTMENT OF PUBLIC WAREHOUSES (SECTION 57)

At any warehousing station, the Assistant or/Deputy Commissioner of Customs may appoint public warehouses wherein dutiable goods may be deposited (Section 57). Goods meant for re-export can be warehoused in these warehouses without payment of duty. The scope and functions of the scheme of appointment of public warehouses as well as the procedure to be followed are normally explained in detail through the Commissionerate's trade notices issued from time to time.

The Government of India's policy in respect of Customs Public Bonded Warehousing is mainly to provide adequate warehousing facilities at selected places in the interior keeping in view the requirement of the trade and industry, the proximity to the ports of import and the availability of Customs expertise. Such public bonded warehouse in inland area are generally managed and controlled by the Central Warehousing Corporation.

2. LICENSING OF PRIVATE WAREHOUSES (SECTION 58)

At any warehousing station, the Assistant or/Deputy Commissioner of Customs may licence private warehouses wherein dutiable goods imported by or on behalf of the licensee or any other imported goods in respect of which facilities for deposit in a public warehouse are not available, may be deposited [Section 58(1)].

The Assistant or/Deputy Commissioner of Customs may cancel a licence granted under Sub-section (1):

- (a) by giving one month's notice in writing to licensee, or
- (b) if the licensee has contravened any provision of this Act or the rules or regulations or committed breach of any of the conditions of licence.

The licensee will, however, be given a reasonable opportunity of being heard, before any licence is cancelled [Section 58(2)].

The Assistant or/Deputy Commissioner of Customs may suspend the licence, pending an enquiry whether a licence granted under Sub-section (1) should be cancelled under Clause (b) of Sub-section (2) [Section 58(3)].

The object of warehousing is to allow the facility to trade of deferring payment of duty on imported goods upto the period permissible under Section 61.

3. WAREHOUSING BOND (SECTION 59)

The importer of any goods specified in Sub-section (1) of Section 61, which have been entered for warehousing and assessed to duty under Section 17 or Section 18 shall execute a bond binding himself in a sum equal to twice the amount of the duty assessed on such goods:

- (a) to observe all the provisions of this Act and the rules and regulations in respect of such goods;
- (b) to pay on or before a date specified in a notice of demand:
 - (i) all duties, and interest, if any, payable under Sub-section (2) of Section 61;
 - (ii) rent and charges claimable on account of such goods under this Act, together with interest on the same from the date so specified at such rate not below eighteen per cent, and not exceeding thirty-six per cent, per annum, as is for the time being fixed by the Central Government, by notification in the Official Gazette; and.
- (c) to discharge all penalties incurred for violation of the provisions of this Act and the rules and regulations in respect of such goods [Section 59(1)].

The Assistant or Deputy Commissioner may permit an importer to enter into a general bond in such amount as the Assistant/ Deputy Commissioner of Customs may approve in respect of the warehousing of goods to be imported by him within a specified period [Section 59(2)].

A bond executed by an importer under this section in respect of any goods shall continue in force notwithstanding the transfer of the goods to any other person or the removal of the goods to another warehouse.

Where whole of the goods or any part thereof are transferred to another person, the proper officer may accept a fresh bond from the transferee in a sum equal to twice the amount of duty assessed on the goods transferred and thereupon the bond executed by the transferor shall be enforceable only for a sum mentioned therein less the amount for which a fresh bond is accepted from the transferee [Section 59(3)].

4. PERMISSION FOR DEPOSIT OF GOODS IN A WAREHOUSE (SECTION 60)

When the provisions of Section 59 have been complied with in respect of any goods, the proper officer may make an order permitting the deposit of the goods in a warehouse (Section 60).

Procedure towards clearance of imported goods for warehousing needs to be explained in brief at this stage.

- *Section 46 of the Customs Act, requires an importer (or his agent) (Custom Broker) to file a Bill of Entry either for Home consumption or for Warehousing.*
- *If an importer intends to deposit his consignment in a private or public (bonded) warehouse he will have to file a Bill of Entry for warehousing (yellow in colour) in quadruplicate in the Import Department of the Custom House/or in Air Cargo Complex.*
- *The Bill of Entry is “noted” in the import manifest of the respective vessel or aircraft and returned to the importer or his agent for presentation in the concerned Appraising/assessing Group in the Custom House/Air Cargo Complex.*
- *The Assessing Officer checks the quantity, value, description etc. of the goods imported and as declared in the Bill of Entry.*
- *He classifies the imported goods in accordance with the Customs Tariff and Central Excise Tariff (for countervailing duty) and indicates the classification and the rates of duties applicable to the goods.*

- *The Bill of Entry so assessed is subject to counter-check by the Group Assistant Commissioner.*
- *After counter check the amount of duty is calculated/quantified and indicated suitably on the Bill of Entry.*
- *In the above process of assessment, the assessing officer also verifies the coverage of the goods by the Import Licence produced, particularly wherever the goods are to be covered by an Import Licence validity. It is pertinent to note that the goods could be permitted to be warehoused only on their Valid Import. Thus, the Import Licence and other connected formalities are also completed.*
- *The Bill of Entry is thereafter returned to the importer.*
- *The importer should execute a bond as required in Section 59 of the Customs Act for twice the amount of duty leviable/balance on the goods.*
- *Instead of executing bonds for each consignment imported, an importer may also furnish a general bond for a lumpsum covering twice the amount of duty leviable on goods to be imported by him during a specified period (6 months, one year, etc.).*
- *The bond Department after completing all the required formalities including acceptance of the double duty bond, will return the warehousing Bill of Entry to the Importer/Customs Broker after stamping the Bill of Entry with an endorsement "returned to the importer". This endorsement on all the copies of the Bill of Entry will also indicate the date on which the Bill of Entry has been returned to the Importer/Customs Broker.*
- *In cases where the Assessing Officer in the Group desires that the goods should be examined or tested before assessment, examination of the goods and verification of fitness for bonding are done by the Docks Air Cargo Appraising Staff.*

Thereafter, the Assessing Officer makes the assessment by indicating the rates of duties applicable to the goods. In such cases the "pass into bond" order is signed by the Preventive Superintendent incharge of the Bonds Department after Assistant Commissioner (Bonds) has accepted the importer's bond for twice the amount of duty payable.

5. PERIOD FOR WHICH GOODS MAY REMAIN WAREHOUSED (SECTION 61)

Sub-section (1) of Section 61 provides that any warehoused goods may be left in the warehouse in which they are deposited or any warehouse to which they may be removed:

- (a) in the case of capital goods intended for use in any hundred per cent export oriented undertaking, till the expiry of five years;
- (aa) in the case of goods other capital goods intended for use in any hundred per cent export-oriented undertaking, till the expiry of three years; and
- (b) in the case of any other goods, till the expiry of one year,

after the date on which the proper officer has made an order under Section 60 permitting the deposit of the goods in a warehouse:

Explanation: For the purposes of this section, "hundred per cent export oriented undertaking" has the same meaning as in Explanation 2 to Sub-section (1) of Section 3 of the Central Excise Act, 1944 (1 of 1944).

Provided that:

- (i) in the case of any goods which are not likely to deteriorate, the period specified in Clause (a) or Clause (aa) or Clause (b) may, on Sufficient cause being shown, be extended—

- (a) in the case of such goods intended for use in any hundred percent export-oriented undertaking by the commissioner of customs, for such period as he may deem fit; and
 - (b) in any other case, by the Commissioner of Customs, for a period not exceeding six months and by the Chief Commissioner of Customs for such further period as he may deem fit.
- (ii) in the case of any goods referred to in Clause (b), if they are likely to deteriorate, the aforesaid period of one year may be reduced by the Commissioner of Customs to such shorter period as he may deem fit.

Provided further that when the licence for any private warehouse is cancelled, the owner of any goods warehoused therein shall, within seven days from the date on which notice of such cancellation is given or within such extended period as the proper officer may allow, remove the goods from such warehouse to another warehouse or clear them for home consumption or exportation.

(2) Where any warehoused goods:

- (i) specified in sub-clause (a) or sub-clause (aa) of Sub-section (1), remain in a warehouse beyond the period specified in that sub-section by reasons of extension of the aforesaid period or otherwise, interest at such rate as is specified in Section 47 shall be payable, on the amount of duty payable at the time of clearance of the goods in accordance with the provisions of Section 15 on the warehoused goods, for the period from the expiry of the said warehousing period till the date of payment of duty on the warehoused goods;
- (ii) specified in sub-clause (b) of Sub-section (1), remain in a warehouse beyond a period of thirty days, interest shall be payable at such rate or rates not exceeding the rate specified in Section 47, as may be fixed by the Board, on the amount of duty payable at the time of clearance of the goods in accordance with the provisions of Section 15 on the warehoused goods for the period from the expiry of the said ninety days till the date of payment of duty on the warehoused goods.

Provided that the Board may, if it considers it necessary so to do in the public interest, by order and under circumstances of an exceptional nature, to be specified in such order, waive the whole or part of any interest payable under this section in respect of any warehoused goods:

Provided further that the Board may, if it is satisfied that it is necessary so to do in the public interest, by notification in the Official Gazette, specify the class of goods in respect of which no interest shall be charged under this section.

6. RELEVANT POINTS TO BE NOTED UNDER SECTION 61

As per Budget 2002, 100% EOUs can deposit capital goods in the Bonded Warehouse for a period beyond 5 years with the permission from the department.

- Interest @ 15% is payable for the goods deposited beyond the permissible period. This is calculated on the amount of duty payable.
- No interest is payable when no duty is finally payable at the time of clearance from the warehouse [Pratibha Processors, 1996. S.C. and National Steel Industries Ltd. (H.C.) 2002].
- For perishable goods, the period of deposit may be 45 days or less.
- When the permission for extension was not granted, the importer has an option to prefer an appeal before CESTAT.

CBEC Circular 15/ 2009 Issue: Whether interest for delayed payment on goods cleared from warehouse after the clearance of B/E is payable as per Section 47(2) of the Act.

Clarification: No, Section 47 is applicable for direct clearance of goods from port area. So, interest provisions under section 47 are not applicable for clearance made from warehouse under Section 68.

Note: Under Section 47(2), interest is payable if the duty is not paid within 2 working days after the clearance of white B/E submitted for clearance for home consumption.

7. WAREHOUSING—GRANT OF EXTENSION IN THE WAREHOUSING PERIOD UNDER SECTION 61 OF THE CUSTOMS ACT, 1962 AFTER EXPIRY OF THE WAREHOUSING PERIOD

1. Section 61 of the Customs Act, 1962 lays down the period for which the imported goods can be warehoused. The first proviso to this section provides that the period of warehousing prescribed, on sufficient cause being shown, can be extended for a period not exceeding 6 months by Commissioner of Customs. Further, extension in the period can be granted by the Chief Commissioner of Customs.
2. A doubt has arisen whether extension in the warehousing period can be granted when the application for extension is moved after the expiry of the initial or extended warehousing period. Section 61 of the Customs Act, 1962 is silent on this issue.
3. In order to arrive at a uniform practice in granting such extensions, the matter was examined in consultation with Ministry of Law. Consequently, it was been decided that the importers may be advised to file such applications for extensions in the warehousing period to the proper authority well before the expiry of initial/ extended period of warehousing.
4. However, in cases of exceptional circumstances, the extensions in the warehousing period can be considered and granted even after the expiry of initial/ extended warehousing period. In all such cases, the jurisdictional Chief Commissioner may himself decide the request for extension after taking into consideration the exceptional circumstances, the nature of the commodity, the rate of duties, particularly, whether the same results in loss of revenue to the government, the licensing aspects involved etc. [M.F. (D.R.) Circular No. 12/98-Cus., dated 6.3.1998].

8. CONTROL OVER WAREHOUSED GOODS (SECTION 62)

Section 62 provides that all warehoused goods shall be subject to the control of the proper officer [Section 62(1)].

No person shall enter a warehouse or remove any goods therefrom without the permission of the proper officer [Section 62(2)].

The proper officer may cause any warehouse to be locked with the lock of the Customs Department and no person shall remove or break such lock [Section 62(3)].

The proper officer shall have access to every part of warehouse and power to examine the goods therein [Section 62(4)].

9. PAYMENT OF RENT AND WAREHOUSE CHARGES (SECTION 63)

Section 63 stipulates that the owner of any warehoused goods shall pay to the warehouse keeper rent and warehouse charges at the rates fixed under any law for the time being in force or where no rates are so fixed at such rates as may be fixed by the Commissioner of Customs [Section 63(1)].

If any rent or warehouse charges are not paid within ten days from the date when they become due, the warehousekeeper, may, after notice to the owner of the warehoused goods, and with the permission of the proper officer, cause to be sold (any transfer of the warehoused goods notwithstanding) such sufficient portion of the goods as the warehousekeeper may select. [Section 63(2)].

10. OWNER'S RIGHT TO DEAL WITH WAREHOUSED GOODS (SECTION 64)

With the sanction of the proper officer, and on payment of the prescribed fees, the owner of any goods may either before or after warehousing the same:

- (a) inspect the goods,
- (b) separate damaged or deteriorated goods from the rest,
- (c) sort the goods or change their containers for the purpose of preservation, sale, export or disposal of the goods,
- (d) deal, with the goods and their containers in such manner as may be necessary to prevent loss or deterioration or damage to the goods,
- (e) show the goods for sale,
- (f) take samples of goods without entry for home consumption and if the proper officer permits, without payment of duty on such samples. (Section 64).

11. MANUFACTURE AND OTHER OPERATIONS IN RELATION TO GOODS IN A WAREHOUSE (SECTION 65)

The owner of any warehoused goods may carry on any manufacturing process or other operations in the warehouse in relation to such goods, with the sanction of Assistant or Deputy Commissioner of Customs and subject to such conditions and on payment of such fees as may be prescribed [Section 65(1)].

Where in the course of any operations permissible in relation to any warehoused goods under Sub-section (1) there is any waste or refuse, the following provisions will apply:

- (a) if the whole or any part of the goods resulting from such operations are exported, import duty shall be remitted on the quantity of the goods contained in so much of the waste or refuse as has arisen from the operations carried on in relation to the goods exported, provided that such waste or refuse is either destroyed or duty is paid on such waste or refuse as if it had been imported into India in that form;
- (b) if the whole or any part of the goods resulting from such operation are cleared from the warehouse for home consumption, import duty shall be charged on the quantity of the warehoused goods contained in so much of waste or refuse as has arisen from the operations carried on in relation to the goods cleared for home consumption [Section 65(2)].

Treatment of Waste and Scrap: Dutiability of scrap is as follows:

Final product exported →	Scrap destroyed /exported →	No duty on either.
Final product exported →	Scrap cleared for home consumption →	Pay import duty on scrap as if scrap has been imported.
Final product cleared for home consumption →	Pay import duty on the entire quantity of goods imported. There is no special treatment for scrap.	

12. POWER TO EXEMPT IMPORTED MATERIALS USED IN THE MANUFACTURE OF GOODS IN WAREHOUSE (SECTION 66)

Under Section 66, if any imported materials are used in accordance with the provisions of Section 65 for the manufacture of any goods and the rate of duty leviable on the imported materials exceeds the rate of duty leviable on such goods, the Central Government, if satisfied that in the interest of the establishment or development of any domestic industry, it is necessary, so to do, may, by notification in the Official Gazette, exempt the imported materials from the whole or part of the excess rate of duty.

13. REMOVAL OF GOODS FROM ONE WAREHOUSE TO ANOTHER (SECTION 67)

The owner of any warehoused goods may with the permission of the proper officer, remove them from one warehouse to another subject to such conditions as may be prescribed for the due arrival of the warehoused goods at the warehouse to which removal is permitted. (Section 67).

The Central Board of Revenue has framed the Warehoused Goods (Removal) Regulations, 1963 for this purpose providing for the following:

(a) Conditions for transport of warehoused goods in the same town — Where the goods are to be removed from one warehouse to another in the same town, proper officer may require that the transport of the goods between the two warehouses be under the supervision of an officer of customs, the owner meeting the cost of such supervision.

(b) Conditions for transport of warehoused goods to another town — Where the goods are to be removed from one warehouse to another in a different town the proper officer may require the person requesting removal to execute a bond in a sum equal to the amount of import duty leviable on such goods and in such form and manner as the proper officer deems fit.

(c) Terms of the bond to be executed — The terms of the bond shall be that if the person executing the bond produces to the proper officer, within three months or within such extended period as such officer may allow, a certificate issued by the proper officer at the place of destination that the goods have arrived at that place the bond shall stand discharged but otherwise an amount equal to the import duty leviable on the goods in respect of which the said certificate is not produced shall stand forfeited.

(d) Surety or security to be furnished — The proper officer may require that the bond shall be with such surety or security or both as is acceptable to him.

14. CLEARANCE OF WAREHOUSED GOODS FOR HOME CONSUMPTION (SECTION 68)

Under Section 68, the importer of any warehoused goods may clear them for home consumption, if:

- (a) a bill of entry for home consumption in respect of such goods has been presented in the prescribed form;
- (b) the import duty leviable on such goods and all penalties, rent, interest and other charges payable in respect of such goods have been paid; and
- (c) an order for clearance of such goods for home consumption has been made by the proper officer.

However that the owner of any warehoused goods may, at any time before an order for clearance of goods for consumption has been made in respect of such goods, relinquish his title to the goods upon payment of rent, interest, other charges and penalties that may be payable in respect of the goods and upon such relinquishment, he shall not be liable to pay duty thereon.

However that the owner of any such warehoused goods shall not be allowed to relinquish his title to such

goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

In the case of BICCO Lawrie Ltd. 2008 (S.C.) it was held that once assessment of warehoused goods is complete and duty liability is discharged, the goods are no longer warehoused goods even-though they are further retained in the warehouse.

In this case the goods (kerosene) were assessed and duty paid. But the goods were not removed from the warehouse. There was a change in the tariff rate at the time of actual removal and the department demanded the duty as per the increased rate. Held that once assessment was over and duty liability was discharged, no further assessment is necessary and no further liability arises.

15. CLEARANCE OF WAREHOUSED GOODS FOR EXPORTATION (SECTION 69)

Any warehoused goods may be exported to a place outside India without payment of import duty, if:

- (a) a shipping bill or a bill of export in the prescribed form or a label declaration accompanying the goods as referred in Section 82 has been presented in respect of such goods;
- (b) the export duty, penalties, rent, interest and other charges payable in respect of such goods have been paid; and
- (c) an order for clearance of such goods, for exportation has been made by the proper officer [Section 69(1)].

Section 69(2) lays down that notwithstanding anything contained in Sub-section (1), if the Central Government is of the opinion that warehoused goods of any specified description are likely to be smuggled back into India, it may, by notification in the Official Gazette, direct that such goods shall not be exported to any place outside India without payment of duty or may be allowed to be so exported subject to such restrictions and conditions as may be specified in the notification.

Important points

Under Section 15(1)(b), the rate of duty applicable to warehoused goods (as and when cleared for home consumption) is the rate of duty prevailing on the date of actual removal of the goods from the warehouse. Hence, the warehouse keeper or Bond Officer endorses the date (or dates) on which the goods are physically removed from the warehouse. If any further duty has become due on account of a change in the rates of duty before such removal, the Bond Clerk who receives the duplicate bill of entry from the warehouse keeper initiates necessary action. More than one clearance of a single warehoused consignment can also be effected by filing different bills of entry (Green Bill of Entry) under Section 68. As far as the rate of exchange (applied for conversion of value declared in foreign currency to Indian currency for collection of duty, on the value) is concerned, the same exchange rate that prevailed and applied for conversion on the date of filing of the warehousing (info-bond) bill of entry by the importer is applicable to all clearances ex-bond.

16. WAREHOUSED GOODS CLEARED AFTER THE EXPIRY OF WAREHOUSING PERIOD - RELEVANT DATE FOR DETERMINING CUSTOMS DUTY

The issue has been considered in the light of Hon'ble Supreme Court's judgment (in Civil Appeal No. 4459 of 1989) delivered on August 23rd, 1996 in the case of Kesoram Rayon v. Commissioner of Calcutta, 1996 (86) E.L.T. 464 (S.C.), 1996 (66) ECR 201 (SC) report. In the said judgement the Hon'ble Apex Court has held that goods which are not removed from a warehouse within the permissible or extended period are to be treated as goods. Importer is required to pay the full amount of duty chargeable at the rate applicable on the

date of their deemed removal from the warehouse, that is, the date on which the permitted or extended period expired.

In other words, a clear interpretation of the Hon'ble Supreme's Court's judgement is that the date of payment of duty in the case of warehoused goods removed after the expiry of the permissible or extended period would henceforth be the date of expiry of the warehousing period or such other extended period as the case may be and not the date of payment of duty. [CBEC Circular No. 31/97-Cus, dated 14.8.1997].

17. ALLOWANCE IN CASE OF VOLATILE GOODS (SECTION 70)

When any warehoused goods to which this section (Section 70) applies are at the time of delivery from a warehouse found to be deficient in quantity on account of natural loss, the Assistant/Deputy Commissioner of Customs may remit the duty on such deficiency [Section 70(1)].

Sub-section (2) of Section 70 lays down that this section applies to such warehoused goods as the Central Government, having regard to the volatility of the goods and the manner or their storage, may, by notification in the Official Gazette specify.

The Government has issued Notification No. 122/63 Cus. dt. 11.5.1963 (as amended), under Sub-section (2), which details such goods namely:

- (1) *aviation fuel, motor spirit, mineral turpentine, acetone, menthol, raw naphtha, vaporising oil, kerosene, high speed diesel oil, batching oil, diesel oil, furnace oil and ethylene dichloride kept in tanks and liquid helium gas kept in containers;*
- (2) *wine, spirit and beer, kept in casks,*

to which the provisions of this section shall apply when they are deposited in a warehouse.

The above provisions in the Customs Act however does not preclude the application of Sections 22 and 23 to warehoused goods (viz.,) for remission of Customs duty on damaged and deteriorated goods and on lost, destroyed and abandoned goods. When any warehoused goods are damaged at any time before clearance for home consumption on account of an account not due to any wilful act, negligence or default of the owner, proportionate abatement of duty is available to the importer. Similarly when any warehoused goods have been lost or destroyed at any time before clearance for home consumption, remission of duty can be allowed by the Assistant Commissioner.

When all the imported goods warehoused have been cleared for home consumption on payment of duty or exported or otherwise duly accounted for, the bond furnished by the importer under Section 59 is cancelled and returned to the importer.

18. PROCEDURE FOR TAKING OUT REMOVAL OF GOODS FROM WAREHOUSE (SECTION 71)

Section 71 provides that no warehoused goods shall be taken out of a warehouse except on clearance for home consumption or re-exportation or for removal to another warehouse or as otherwise provided by this Act.

19. GOODS IMPROPERLY REMOVED FROM WAREHOUSE ETC. (SECTION 72)

Section 72 lays down provisions in respect of goods improperly removed from warehouse etc.

In any of the following cases, that is to say —

- (a) Where any warehoused goods are removed from a warehouse in contravention of Section 71;

- (b) Where any warehoused goods have not been removed from a warehouse at the expiration of the period during which such goods are permitted under Section 61 to remain in a warehouse;
- (c) Where any warehoused goods have been taken under Section 64 as samples without payment of duty;
- (d) Where any goods in respect of which a bond has been executed under Section 59 and which have not been cleared for home consumption or exportation are not duly accounted for to the satisfaction of the proper officer;

the proper officer may demand and the owner of such goods forthwith pay the full amount of duty chargeable on account of such goods, together with all penalties, rent, interest, and other charges payable in respect of such goods [Section 72(1)];

If any owner fails to pay amount demanded under Sub-section (1), the proper officer may, without prejudice to any other remedy, cause to be detained and sold, after notice to the owner (any transfer of the goods notwithstanding) such sufficient portion of his goods, if any, in the warehouse, as the said officer may select.

20. CANCELLATION AND RETURN OF WAREHOUSING BOND (SECTION 73)

Section 73 lays down that when the whole of goods covered by any bond executed under Section 59 have been cleared for home consumption or exported or are otherwise duly accounted for and when all amounts due on account of such goods have been paid, the proper officer shall cancel the bond as discharged in full and shall on demand deliver it, so cancelled, to the person who had executed or is entitled to receive it.

CASE STUDIES

SBEC SUGAR LTD. 2011 (S.C.) – (Warehousing- delayed clearance)

Facts: The importer was to remove goods from warehouse on 25-12-1996. Department issued demand notice under Section 72 of Customs Act for removal. The importer filed B/E on 21st Jan 1998. The duty was nil by exemption notification at the time of submission of B/E (21st Jan 1998.)

Issue: What is the relevant date for rate of duty.

Contentions: The importer argued that relevant date for rate of duty as per Section 15(1) (b) is date of submission of Green Bill of Entry. Since rate of duty applicable on that date is nil by exemption, no duty is payable.

Department: Section 68 and Section 15 are applicable to cases for proper removal of goods. This is a case of improper removal governed by Section 72. Hence, rate of duty applicable shall be the one prevailing at the official due date of removal ie. 25-12- 1996 and not 21st Jan 1998. Hence, duty is payable.

Decision: The contention of the department is correct and the rate applicable on the deemed (due) date of removal shall be taken for assessment.

DECORATIVE LAMINATES (I) PVT. LTD. 2010 (H.C)–(Remission on warehoused goods)

Facts: The goods were deposited in a warehouse and due to lack of demand, extension was sought and granted. Even the extended period was over by 31st Dec 2001. Still the goods were not removed. In the meantime the goods were destroyed in the warehouse. Then the importer applied for remission under Section 23 of the Act.

Held: **No remission** under Section 23 of the Customs Act for warehoused goods if they are lost or destroyed in the warehouse after the expiry of warehousing period.

Further held that the benefit of **remission under Section 23 is available only to proper removals.**

Illustration

Bholaram imported certain goods in November, 2011 and an 'into bond' bill of entry was presented on 28th November, 2011. Assessable value was US \$1,00,000. Order permitting the deposit of goods in warehouse for 3 months was issued on 2nd December, 2011. Bholaram neither obtained extension of warehousing period nor cleared the goods within the permitted warehousing period of 1st March, 2012. Only after a notice was issued under section 72 of the Customs Act, 1962 demanding duty and other charges, Bholaram removed the goods on 15th April, 2012.

Compute the amount of duty payable by Bholaram while removing the goods from warehouse, assuming that no additional duty or special additional duty is payable. You are supplied with the following information:

	28.11.2011	01-03.2012	15.04.2012
Rate of exchange per US \$	₹56	₹55	₹54
Rate of basic customs duty	15%	10%	5%

Solution:

Assessable value is	₹56,00,000
Add: BCD @ 10%	5,60,000
Add: Cess @3% on BCD	<u>16,800</u>
Total duty payable	<u>576,800</u>

Rate of Exchange: ₹56; Rate of basic custom duty: 10 %;

II. DUTY DRAWBACK (SECTION 74 TO 76)

Indirect taxes are taxes on domestic consumption. They are destination based. Goods exported shall be free from local taxes. It is in tune with the slogan 'export goods and services, don't export taxes'. To implement the policy, govt of India introduced export promotion schemes making the exports tax free. Duty Drawback scheme is an export promotion scheme under customs. Sections 74 to 76 deal with duty drawback scheme.

Under the scheme, if import duty paid goods are exported with or without any value addition, the import duties and other taxes paid on such goods at input level are refunded in the form of duty drawback. Duty drawback is basically a refund of import duties. There are two variants of duty drawback scheme under Customs.

1. Re-exportation of duty paid imported goods [Section 74]
2. Export of final products/ processed goods using duty paid imported material [Section 75]

In both the cases, there are three common features.

- (i) There is import of some goods;
- (ii) The imported goods suffered import duty;
- (iii) The same goods in same form or in a different form have been exported.

STATUTORY PROVISIONS IN THE CUSTOMS ACT, 1962

The provisions relating to drawback are enumerated in Chapter X, in Sections 74, 75, 75A and 76 of the Customs Act, 1962. Drawback is allowed subject to conditions mentioned in Sections 74 to 76 and notifications issued thereunder, in respect of duty paid on:

- (a) imported goods, which are re-exported as such (without use),
- (b) imported goods, which are re-exported after use,
- (c) imported material used in the manufacture of goods exported.

DRAWBACK ALLOWABLE ON RE-EXPORT OF DUTY PAID GOODS (SECTION 74)

The elements necessary to consider a claim for Drawback under Section 74 Customs Act, 1962 are:

- (i) The goods on which the drawback is claimed must have been previously imported;
- (ii) Import duty must have been paid on these goods when they were imported;
- (iii) The goods must be entered for re-export within two years from the date of payment of duty. However, it is provided that in any particular case this period of two years may, on sufficient cause being shown, be extended by the Board by such further period it may deem fit;
- (iv) The goods are identified to the satisfaction of the Assistant Commissioner of Customs as the goods that were imported;
- (v) The goods must be actually re-exported to any place out-side India;
- (vi) The goods must be capable of easy identification; and
- (vii) The market price of such goods must not be less than the amount of drawback claimed.

The Central Government has been empowered to make rules for the purpose of carrying out the provisions of Section 74 and, in particular, such rules may:

- (a) provide for the manner in which the identity of goods imported in different consignments which are ordinarily stored together in bulk, may be established;
- (b) specify the goods which shall be deemed to be not capable of being easily identified; and
- (c) provide for the manner and the time within which a claim for payment of drawback is to be filed."

RE-EXPORT OF IMPORTED GOODS (DRAWBACK OF CUSTOMS DUTIES) RULES, 1995

In exercise of the powers conferred under the amended Rule 74 [under clause (c) of Sub-section (3) of Section 74, above], the Central Government has framed the Re-export of Imported Goods (Drawback of Customs Duties) Rules, 1995. These rules have been issued specifying the procedure for filing a claim in respect of goods exported under a claim for drawback under Section 74 as it had become necessary to prescribe a procedure for filing of a claim in view of Section 75A of the Customs Act which now requires the Government to pay interest at the specified rates in case drawback is not paid to the exporter within one month from the filing of his claim.

Rates of Drawback of Import Duty Admissible under Section 74

Two types of cases are covered in the above category. They are:

- (i) *Imported goods exported as such, without putting into use — the drawback given is 98% of duty paid on import. (The idea behind withholding 2% is to cover administrative expenses).*
- (ii) *Imported goods exported after use.*

If the goods had been used after import and then exported the rate of drawback i.e. the percentage of duty refunded will be according to the period of usage, between the date of clearance for home consumption and the date when the goods are “placed under Customs Control” for exports. The rate of drawback in this case is not fixed and progressively decreases as the period of use increases as enumerated in Customs Notification No. 19 dated 6.2.1965 as amended by Customs Notification No. 45/70 dated 2.5.1970. In satisfying the condition “placed under Customs Control”, it is necessary that the “Shipping Bill” should be filed and the goods “physically brought in to Customs area” for export and placed under the control of Customs.

Customs Notification No. 19 dated 6.2.1965 (as amended) while setting out the rates of drawback, differentiates as between two categories of goods, in the grant of drawback:

- (i) Goods imported by a person for his personal and private use and motor cars; and
- (ii) Other goods

(i) Goods imported by a person for his personal and private use and motor cars:

The goods imported by a person for his personal and private use, may be exported as “baggage” and he shall make a declaration, (Baggage declaration - the format used for clearance of unaccompanied baggage) which declaration shall be deemed to be an “Entry for Export”.

The drawback rates are calculated, by reducing the Import duty paid by 4%, 3%, 2-1/2% and 2% for use, for each quarter or part thereof during the period of First, Second, Third and Forth year respectively.

Even though the rates are provided as above, in the notification, for grant of drawback for goods imported for personal and private use, and used for more than 2 years, the Commissioner of Customs could grant extension of time limit (beyond two years) but no drawback is admissible beyond 4 years.

On the category of goods covered by (b) above,

(ii) Other goods: *In this case, the percentage of import duty payable as drawback depends on the period of usage of such goods as detailed below:*

Rate fixed by Government under Section 74(2) by Notification No. 23/2008-Cus., dt. 1.3.2008.

Period of use	Draw Back Rate
Not more than 3 months	95%
3-6 months	85%
6-9 months	75%
9-12 months	70%
12-15 months	65%
15-18 months	60%
Above 18 months	NIL

For Motor Vehicles

Use per quarter during	Percentage of Reduction
1st Year	4%
2nd Year	3%
3rd Year	2.5%
4th Year	2%

For use over 24 months extension of time-limit by the Commissioner is required before grant of drawback.

Also drawback shall not be given on the following goods if used after their importation:

- (i) Wearing apparel.
- (ii) Tea-chests.
- (iii) Exposed cinematograph films passed by the Board of Film Censors in India.
- (iv) Unexposed photographic films, paper and plates and X-ray films.

DRAWBACK ON IMPORTED MATERIALS USED IN THE MANUFACTURE, PROCESSING OR OPERATION OF GOODS WHICH ARE EXPORTED (SECTION 75)

As distinct from Section 74 of the Customs Act, 1962, Section 75 postulates repayment of a part or whole of the duty paid on materials imported and used in manufacturing of goods which are exported as manufactured items outside India. Section 75 has been amended by the Finance Act, 1995 to permit drawback not only on materials/inputs used in the manufacture but also processed or subjected to any other operation for export of goods from India. The amendment is made to overcome the difficulty caused by the restricted meaning of the word "manufacture" in Section 75(1) of the Customs Act.

Drawback, as the name itself suggests, particularly with reference to Section 75 of the Customs Act, 1962, is a procedure to relieve the export goods of duties borne by goods at various stages of their manufacture, processing or any other operation carrying out on them. Such relief is allowed in respect of duties paid on raw-materials, and components utilised in the manufacture, processing etc. of goods. The wastages involved in the manufacture, processing etc. and the duty incidence(s) on the packing materials used in the Export of the goods are also taken into account. Drawback is allowed not only on duties incurred in the "Direct Imports" of materials or components utilised in the manufacture, processing etc. of Export goods but also on earlier inputs that go into the raw-materials and manufacture, processing etc. of components. Therefore, the rates of drawback are fixed by the Government on "average basis", on the basis of the relevant data obtained from the leading manufacturers or the persons carrying out any process or any other operation either for a class of goods or for specific goods. The procedure set out in Section 75 of Customs Act, 1962, as reproduced hereunder, the Customs and Central Excise Duties Drawback Rules, 1995 allow of drawback, of Customs duties and Central Excise duties that are chargeable on imported and indigenous materials respectively, used in the manufacture, processing or any other operation carried out on goods exported under claim for Drawback.

DRAWBACK ON IMPORTED MATERIALS USED IN THE MANUFACTURE OF GOODS WHICH ARE EXPORTED (SECTION 75)

- (1) Where it appears to the Central Government that in respect of goods of any class or description manufactured, processed or on which any operation has been carried out in India, being goods which have been entered for export and in respect of which an order permitting the clearance and loading thereof for exportation has been made under Section 51 by the proper officer, or being goods entered for export by post under Section 82 and in respect of which an order permitting clearance for exportation has been made by the proper officer, a drawback should be allowed of duties of customs chargeable under this Act on any imported materials of a class or description used in the manufacture or processing of such goods or carrying out any operation on such goods, the Central Government may, by notification in the Official Gazette, direct that drawback shall be allowed in respect of such goods in accordance with land subject to the rules made under Sub-section (2).

Provided that no drawback shall be allowed under this sub-section in respect of any of the aforesaid

goods which the Central Government may, by rules made under Sub-section (2), specify, if the export value of such goods or class of goods is less than the value of the imported materials used in the manufacture or processing of such goods or carrying out any operation on such goods or class of goods, or is not more than such percentage of the value of the imported materials used in the manufacture or processing of such goods or carrying out any operation on such goods or class of goods as the Central Government may, by notification in the Official Gazette, specify in this behalf:

Provided further that where any drawback has been allowed on any goods under this sub-section and the sale proceeds in respect of such goods are not received by or on behalf of the exporter in India within the time allowed under the Foreign Exchange Management Act 1999, such drawback shall except under such circumstances as the central government may, by rules, specify be deemed never to have been allowed and the Central Government may, by rules made under Sub-section (2), specify the procedure for the recovery or adjustment of the amount of such drawback.

- (1A) Where it appears to the Central Government that the quantity of a particular material imported into India is more than the total quantity of like material that has been used in the goods manufactured processed, or on which any operation has been carried out in India and exported outside India, then, the Central Government may, by notification in the Official Gazette, declare that so much of the material as is contained in goods exported shall, for the purpose of Sub-section (1), be deemed to be imported material.
- (2) The Central Government may make rules for the purpose of carrying out the provisions of Sub-section (1) and, in particular, such rules may provide:
 - (a) for the payment of drawback equal to the amount of duty actually paid on the imported materials used in the manufacture or processing of the goods or carrying out any operations on the goods or as is specified in the rules as the average amount of duty paid on the materials of that class or description used in the manufacture or processing of export goods or carrying out any operation on export goods of that class or description either by manufacturers generally or by persons processing or carrying on any operation generally or by any particular manufacturer or particular person carrying on any process or other operation and interest if any, payable thereon;
 - (aa) for specifying the goods in respect of which no drawback shall be allowed;
 - (ab) for specifying the procedure for recovery or adjustment of the amount of any drawback which had been allowed under Sub-section (1) or interest chargeable thereon.
 - (b) for the production of such certificates, documents and other evidence in support of each claim of drawback, as may be necessary;
 - (c) for requiring the manufacturer or the person carrying on any process or any other operation to give access to every part of his manufactory to any officer of customs specially authorised in this behalf by the Assistant Commissioner of Customs to enable such authorised officer to inspect the process of Manufacture, process or any other operations carried out and to verify by actual check or otherwise the statements made in support of the claim for drawback.
 - (d) for the manner and the time within which claim for payment of drawback may be filed;
- (3) The power to make rules conferred by Sub-section (2) shall include the power to give drawback with retrospective effect from a date not earlier than the date of changes in the rates of duty on inputs used in export goods.

PAYMENT OF INTEREST ON DRAWBACK (SECTION 75A)

Section 75A of the Customs Act provide for levy of interest on delayed payment of drawback. Interest at such rate as may be fixed by the Board would be allowed in case payment against a claim for drawback is not made within one* month of filing the claim in the prescribed manner. Likewise, when a drawback claim has been allowed erroneously, interest at the prescribed rate would be payable if the excess amount is not deposited with the Government within one month of the amount being demanded.

Section 75A reads thus:

- 75A (1) Where any drawback payable to a claimant under Section 74 or Section 75 is not paid within a period of *one month from the date of filing a claim for payment of such drawback, there shall be paid to that claimant in addition to the amount of drawback, interest at the rate fixed under Section 27A from the date after the expiry of the said period of *one month till the date of payment of such drawback.
- (2) Where any drawback has been paid erroneously or it becomes otherwise recoverable under the Act or the rules made thereunder, the claimant shall, within a period of two months from the date of demand, pay interest. The amount of interest shall be calculated from the date of payment of such drawback to the claimant till the date of recovery of such drawback. [Section 75A(2)].

PROHIBITION AND REGULATION OF DRAWBACK IN CERTAIN CASES (SECTION 76)

Independent of other conditions which are laid down in Sections 74 and 75 of Customs Act, 1962 and in the Drawback Rules, no drawback will be granted:

- (a) in respect of any goods the market price of which is less than the amount of drawback due thereon; and
- (b) where drawback due on any goods is less than ₹ 50.

Also, if the Central Government is of opinion that specified goods on which drawback is claimed are likely to be smuggled back into India, it may stipulate that drawback be paid subject to certain conditions. There are three notifications in this regard:

Notification 50/63 dt. 1.2.63 as amended by 153/68 dt. 29.10.68 lays down that goods if exported on vessels less than 1,000 tons are likely to be smuggled back into India than export under claim for drawback may be permitted on the following conditions:

- (i) The agent of the vessel executes a bond in a sum equal to the amount of drawback and in such form and manner as the proper officer deems fit. The terms of the bond shall be that if the agent of the vessel produces to the proper officer, within three months or within such extended period as the proper officer may allow, a certificate issued by the Customs authorities at the port of destination that the goods have been landed at the port the bond shall stand discharged; but otherwise a sum equal to the amount of drawback allowed on the goods in respect of which the said certificate is not produced shall stand forfeited. The above bond shall be with such surety or security or both as is required by the Customs.
- (ii) The exporter produces to the proper officer a certificate issued by the Customs Authorities at the port of destination that the goods have been landed at the port or a certificate from the authorised dealer.

Under Notification 51/1.2.63 the following goods put on board a vessel less than 200 tons for use as stores are not to be given drawback:

- (i) alcoholic liquors;
- (ii) cigarettes;
- (iii) cigars;
- (iv) pipe tobacco.

Notification 208/1.10.77 lays down that drawback is not to be allowed on exports to Bhutan, Nepal or by land to Burma, Tibet or Sikiang except on certain conditions given in the said Notification.

CUSTOMS AND CENTRAL EXCISE DUTIES DRAWBACK RULES, 1995

The duty drawback scheme is presently administered by the Directorate of Drawback in the Ministry of Finance. Drawback on exports is sanctioned and paid by the concerned Commissioner of Customs or Central Excise incharge of the port/airport/Land Customs Station through which the goods are exported, at the rates determined by the Directorate. These drawback rates are fixed either for a class of products manufactured in the country which are available to all exporters, and known as All-industry Rates or for a product of a particular manufacturer — known as Brand Rate. The rates are reviewed and revised periodically taking due note of variation in consumption pattern of inputs and duties suffered thereon. The Drawback is admissible irrespective of mode of export i.e. whether despatched by Sea, Air, Land Customs Station or Parcel Post.

Pursuant to the amendments made in sections dealing with drawback in the Customs Act and to streamline the existing rules, it was considered necessary to revise the Customs and Excise Duties Drawback Rules, 1971. Accordingly, Customs and Central Excise Duties Drawback Rules, 1995 were issued in supersession of 1971 Rules.

PROCEDURE FOR FIXATION OF ALL-INDUSTRY RATES

Under Rule 3 of the Drawback Rules, the Central Government determines the rate(s) of drawback in respect of certain classes of goods and notifies the same through public notices. Any exporter of these goods can claim Drawback at All Industry Rates. He is, however unless otherwise specifically provided, debarred from availing these rates as per General Notes laid down in the relevant Public Notice issued annually if he has been otherwise permitted certain concessions e.g. facility of manufacture in Bond, duty free imports under Advance Licensing/Import-Export Pass Book Scheme, facility of exports under Central Excise Rules, etc. (In such cases, for any unrebated customs or central excise duties, facility of Brand Rates is generally provided).

All Industry rates are reviewed by the Government annually, taking due note of Budgetary changes and revised wherever necessary, taking into account the changes in the duty incidence consequent to changes in the rate of Customs or Central Excise Duties and or the variations in the prices of various inputs (where the rates of duties are ad valorem). The revised All Industry Rates are generally made effective from 1st June and are normally kept unchanged for 1 year. If changes in duties on basic inputs of a product at any point of time (after the presentation of Budget) are substantial, the corresponding All industry Rates are reviewed and appropriate change is also effected in between the year. From time to time new products are also added to the list of goods having All Industry Rates.

In determining the All Industry Rates, for a particular class of goods, as per Rule 3(2) of Drawback Rules, the Central Government takes into account the following:

- (i) the average quantity or value of each class or description of the materials from which a particular class of goods are ordinarily produced or manufactured in India;
- (ii) the average quantity or value of the Imported material or excisable materials used for production or manufacture in India;
- (iii) the average amount of duties paid on Imported materials or excisable materials used in the manufacture of the semis, components and intermediate products used in the manufacture;
- (iv) the average amount of duties paid on materials wasted in the manufacturing process and catalytic agents (If such waste or catalytic agent is re-used in any process of manufacture or sold, the average amount of the duties on the waste or catalytic agent re-used/sold shall be deducted);
- (v) the average amount of duties paid on imported materials or excisable materials used for containing or packing the export product; and
- (vi) any other information considered relevant for determining the drawback rate.

BRAND RATES

Where the Central Government has not determined the All Industry rates of drawback in respect of any export product eligible for such drawback (set out in Schedule to the Drawback Rules), or where the rate is not eligible because the manufacturer of the product has availed of certain duty free facilities (like Advance Authorization) but where sufficient duty paid inputs are also used, any manufacturer or exporter of such goods may apply under Rule 6 of the Drawback rules to the Central Government for the determination of the drawback rate for his product of specified description/characteristics.

SPECIAL BRAND RATES

In case any manufacturer/exporter finds that the All industry rate of drawback for any class of goods is less than four-fifth of the duties paid on the materials or components used in the production/manufacture and packing of same goods being exported by him, he can make an application for fixation of an appropriate amount or rate of drawback (under Rule 7 of the Drawback Rules) for his products of specified description/characteristics. Such rates, wherever determined, are termed as 'Special Brand Rates'.

PROVISIONAL RATE OF DRAWBACK

Exporters have also the facility to apply for fixation of a provisional drawback rate as per provisions of Rule 6(2)(a) of Drawback Rules, in cases where they have already applied for fixation of brand rates/special brand rates of their products whose finalisation is pending. The payment at provisional rates is, however, subject to execution of a suitable bond (with surety/security) by the Exporter with the concerned Custom House. On finalisation of the rate, the differential amount is appropriately adjusted.

MINIMUM RATE OF DRAWBACK

As per Rule 8 of the Drawback Rules, for any export product where the duties paid on inputs work out to less than 1% of F.O.B. value thereof (except where the amount of drawback per shipment exceeds rupees Five hundred), no Drawback rate (All-industry Rate or Brand Rate) is determined. However, this condition of minimum 1% of F.O.B. value will not be applicable in case exports are made by post and exports are made in discharge of obligation against Advance authorization issued under Duty Exemption Scheme. Thus, in case of exports made by post and exports under Duty Exemption Scheme, drawback shall be payable in all cases wherever the amount of drawback is more than ` 50/-, the minimum limit specified statutorily in Section 76 of the Customs Act.

Further, under sub-rule (2), of Rule 8 it is provided that no amount or rate of drawback shall be determined in

respect of any goods or class of goods under Rule 6 or Rule 7, as the case may be, if the export value of each of such goods or class of goods in the bill of export or shipping bill is less than the value of the imported materials used in the manufacture of such goods or class of goods, or is not more than such percentage of the value of the imported materials used in the manufacture of such goods or class of goods as Central Government may, by notification in the Official Gazette, specify in this behalf.

An 'Explanation' added to Sub-rule (2) provides that "Export Value" in relation to any export goods means the value thereof, determined in accordance with the provisions of Sub-section (1) of Section 14 of the Customs Act, 1962.

Customs, Central Excise Duties, Service Tax Drawback Rules, 1995, students may refer to the latest Customs Law Manual.

In *U.O.I. v. Rajindra Dyeing and Printing Mills, 2005 (180) ELT 433 (SC)* it was held that export is complete when goods cross territorial waters of India. If ship sinks within territorial waters, export is not complete and DDBK not payable.

III. BAGGAGE (SECTION 77 TO 81)

Chapter XI of the Customs Act, 1962 contains special provisions regarding baggage, goods imported or exported by post and stores. This Chapter is divided into three Parts,

- Part I deals with baggage (Sections 77 to 81),
- Part II deals with goods imported or exported by post (Sections 82, 83 and 84), and
- Part III deals with Stores (Sections 85 to 90).

These provisions are discussed herein below:

DECLARATION BY OWNER OF BAGGAGE [SECTION 77]

Section 77 provides that the owner of any baggage shall for the purpose of clearing it make a declaration of its contents to the proper officer.

The word 'baggage' is a comprehensive term which means luggage of a passenger accompanied or unaccompanied and comprises of the trunks or bags and the personal belongings of the passenger contained therein. It is in this comprehensive sense that the term "baggage" has been used in Sections 77 and 80 of the Customs Act. Thus, 'baggage' has been given a larger and ordinary meaning. (*Union of India v. Khalil Kecherim, 1970 Cri. L.J. 417*).

Section 2(3) of the Customs Act defines baggage as including unaccompanied baggage but excluding motor vehicle.

DETERMINATION OF RATE OF DUTY AND TARIFF VALUATION IN RESPECT OF BAGGAGE [SECTION 78]

According to Section 78 of the Customs Act, 1962, the rate of duty and tariff-valuation, if any, applicable to baggage shall be the rate and valuation in force on the date on which a declaration is made in respect of such baggage under Section 77.

BONA-FIDE BAGGAGE EXEMPT FROM DUTY [SECTION 79]

Section 79(1) provides that the proper officer may, subject to any rules made under Sub-section (2) pass free of duty —

- (a) Any article in the baggage of a passenger or a member of the crew in respect of which the said

officer is satisfied that it has been in use for such minimum period as may be specified in the rules.

- (b) Any article in the baggage of a passenger in respect of which the said officer is satisfied that it is for the use of the passenger or his family or is a bona-fide gift or souvenir.

Provided that the value of each such article and the total value of all such articles does not exceed such limits as may be specified in the rules [Section 79(1)].

The Central Government may make rules for the purpose of carrying out the provisions of this section and in particular, such rules may specify -

- (a) the minimum period for which any article has been used by a passenger or a member of the crew for the purpose of clause (a) of Sub-section (1).
- (b) the maximum value of any individual article and the maximum total value of all the articles which may be passed free of duty under clause (b) of Sub-section (1).
- (c) the conditions (to be fulfilled before or after clearance), subject to which any baggage may be passed free of duty. [Section 79(2)].

Section 79(3) lays down that different rules may be made under Sub-section (2) for different classes of persons.

In the Act a distinction has been made between 'baggage' and 'bona-fide baggage' which is exempt from customs duty and in respect of which the proper officer has been empowered to pass free of duty any article which is in the baggage of a passenger and which has souvenir. Therefore, any article in the baggage of a passenger, even though it may be 'goods' within the meaning of Section 2(22) of the Act, will be allowed to be imported free of duty, if it is passed under Section 79 of the Act.

The Government of India in the Ministry of Finance, Department of Revenue and Excise has in exercise of powers conferred by Sub- section (2) of Section 79 framed the Baggage Rules, 1998, the Tourist Baggage Rules, 1998 and the Transfer of Residence Rules, 1978. The text of these rules is given in Annexure 1 to this Study.

TEMPORARY DETENTION OF BAGGAGE [SECTION 80]

Section 80 of the Customs Act, provides that, where the baggage of a passenger contains any article which is dutiable or the import of which is prohibited and in respect of which a true declaration has been made under Section 77, the proper officer may at the request of the passenger, detain such article for the purpose of being returned to him on his leaving India.

REGULATION IN RESPECT OF BAGGAGE [SECTION 81]

Baggage is exempt from CVD. However, education cess@2% and Secondary and higher education cess @1% is payable. Section 81 lays down that the Board may make regulations:

- (a) providing for the manner of declaring the contents of any baggage;
- (b) providing for the custody, examination, assessment to duty and clearance of baggage;
- (c) providing for the transit or transhipment of baggage from one customs station to another or to a place outside India.

The Government of India, Department of Revenue and Excise has framed:

- (i) Baggage Rules 1998;
- (ii) Tourist Baggage Rules 1978;

(iii) Transfer of Residence Rules, 1978.

(1) Baggage includes unaccompanied baggage but does not include motor vehicles [section 2(3)].

Baggage includes all dutiable articles imported by passenger or crew but does not include motor vehicles, alcoholic drinks (beyond limits) and goods imported through courier.

(2) Duty free allowances generally allowed to the Indian resident or foreigner residing in India:

- For Indian resident or a foreigner residing in India and returning from countries other than Nepal, Bhutan, Myanmar or China through other than by specified land route:

Duty Free allowance for bona fide baggage consisting of	For passengers of age 10 years and above		For passengers of age below 10 years	
	Stay abroad for more than 3 days	Stay abroad for 3 days or less	Stay abroad for more than 3 days	Stay abroad for 3 days or less
Used personal effects (excluding jewellery) required for satisfying daily necessities of life	Free	Free	Free	Free
Articles other than those mentioned below at note no.(b) if carried on person or in the accompanied baggage	Free upto ₹35,000.	Free upto ₹15,000.	Free upto ₹ 6,000.	Free upto ₹3,000.

- For Indian resident or a foreigner residing in India and returning from countries from Nepal, Bhutan, Myanmar or China other than by specified land route or for Indian resident or a foreigner residing in India and returning from countries other than Nepal, Bhutan, Myanmar or China by specified land route:

Duty Free allowance for bona fide baggage consisting of	For passengers of age above 10 years and Stay abroad for more than 3 days	For passengers of age upto 10 years and Stay abroad for more than 3 days
Used personal effects (excluding jewellery) required for satisfying daily necessities of life	Free	Free
Articles other than those mentioned at note no.(b) if carried on person or in the accompanied baggage	Free upto ₹ 6,000.	Free upto ₹ 1,500.

Note:

- The free allowance shall not be allowed to be pooled with the free allowance of any other passenger.
- The free allowance is not applicable to the following goods:
 - Fire arms.
 - Cartridges of fire arms exceeding 50.
 - Cigarettes exceeding 200 or cigars exceeding 50 or tobacco exceeding 250 gms.

- (iv) Alcoholic liquor and wines in excess of 2 litre each.
- (v) Gold or silver, in any form, other than ornaments.
- (c) The goods over and above the free allowances shall be chargeable to **customs duty @ 35% + an education cess of 3% i.e. to say the effective rate is 36.05%**.
- (d) In case the value of one item exceeds the duty free allowance, the duty shall be calculated only on the excess of such amount.

(3) Import of gold and silver as baggage

An Indian passenger who has been residing abroad for over one year is allowed to bring jewellery, free of duty in his bonafide baggage upto an aggregate value of ₹ 50,000/- (in the case of a gentleman passenger) or ₹1,00,000/- (in the case of a lady passenger).

(4) Transfer of residence (TR)

A person who is transferring his residence to India shall be allowed clearance free of duty, in addition to allowances applicable to Indian residents or foreigners residing in India or to passengers returning from Nepal, Bhutan, Myanmar or China, other than by specified land route articles in bonafide baggage to the extent and subject to conditions as mentioned below :

Articles allowed Free of Duty	Conditions	Relaxation that may be considered
(a) Used personal and household articles other than those listed at Annex I* or Annex II**, but including (the articles listed at Annexure-III***) and Jewellery upto ₹50,000 by a gentleman passenger or ₹1,00,000 for a lady passenger	<ul style="list-style-type: none"> (1) Minimum stay of two years abroad, immediately preceding the date of his arrival on transfer of residence (2) Total stay in India on short visits during the 2 preceding years should not exceed 6 months, and (3) Passenger has not availed this concession in the preceding three years. 	<ul style="list-style-type: none"> (a) For condition (1) Shortfall of upto 2 months in stay abroad can be condoned by Deputy/Assistant Commissioner of Customs if the early return is on account of - <ul style="list-style-type: none"> (i) terminal leave or vacation being availed of by the passenger, or (ii) any other special circumstances. (b) For condition (2) Commissioner of Customs may condone short visits in excess of 6 months in deserving cases. (c) For condition (3) No relaxation.
(b) Jewellery taken out earlier by the passenger or by a member of his family from India.	Satisfaction of the Assistant Commissioner of Customs regarding the jewellery having been taken out earlier from India.	-----

*** Annexure I**

1. Fire arms.
2. Cartridges of fire arms exceeding 50.

3. Cigarettes exceeding 200 or cigars exceeding 50 or tobacco exceeding 250 gms.
4. Alcoholic liquor or wines in excess of 2 litres.
5. Gold or silver, in any form, other than ornaments.
6. Flat Panel (LCD/LED/Plasma) Television

****Annexure II**

1. Colour Television or Monochrome Television.
2. Digital Video Disc Player.
3. Video Home Theatre System.
4. Dish Washer.
5. Music System.
6. Air Conditioner.
7. Domestic refrigerators of capacity above 300 litres or its equivalent.
8. Deep Freezer.
9. Microwave Oven.
10. Video camera or the combination of any such video camera with one or more of the following goods, namely:-
 - (a) Television Receiver;
 - (b) Sound recording or reproducing apparatus;
 - (c) Video reproducing apparatus.
11. Word Processing Machine.
12. Fax Machine.
13. Portable Photocopying Machine.
14. Vessel.
15. Aircraft.
16. Cinematographic films of 35 mm and above.
17. Gold or Silver, in any form, other than ornaments.

*****Annexure III**

1. VCR or VCP or VTR or VCDP.
2. Washing Machine
3. Electrical or LPG Cooking Range
4. Personal Computer (Desktop Computer)
5. Lap Top Computer (Notebook Computer)
6. Domestic Refrigerator upto 300 Ltr. Capacity or its equivalent.

(5) Baggage by foreign tourist coming to India and currency he can bring in

A tourist is a passenger

- (a) who is not normally a resident in India;

- (b) who enters India for a stay of not more than six months in the course of any twelve months period for legitimate non-immigrant purposes, such as : touring, recreation, sports, health, family reasons, study, religious pilgrimage, or business;

A tourist arriving in India shall be allowed clearance free of duty articles in his bonafide baggage to the extent as mentioned below:-

Persons	Articles allowed free of duty
Tourists of Indian origin other than tourist of India coming by specified land route.	<p>(i) Used personal effects and travel souvenirs, if-</p> <p>(a) These goods are for personal use of the tourist, and</p> <p>(b) These goods, other than those consumed during the stay in India, are re-exported when the tourist leaves India for a foreign destination.</p> <p>(ii) duty free allowances for articles as specified on Question no.</p>
Tourists of foreign origin other than those of Nepalese origin coming from Nepal or of Bhutanese origin coming from Bhutan or of Pakistani origin coming from Pakistan.	<p>(i) Used personal effects and travel souvenirs, if</p> <p>(a) These goods are for personal use of the tourist, and</p> <p>(b) These goods, other than those consumed during the stay in India, are re-exported when the tourist leaves India for a foreign destination.</p> <p>(ii) Articles upto a value of ₹ 8000/- for making gifts.</p>
Tourists of Nepalese origin coming from Nepal or of Bhutanese origin coming from Bhutan.	No free allowance.
Tourists of Pakistani origin coming from Pakistan other than by land route or Pakistan origin of foreign tourists coming from by specified land route Indian origin coming by specified land route	<p>(i) Used personal effects and travel souvenirs, if</p> <p>(a) These goods are for personal use of the tourist, and</p> <p>(b) These goods, other than those consumed during the stay in India, are re-exported when the tourist leaves India for a foreign destination.</p> <p>(ii) Articles upto a value of ₹6000 for making gifts.</p>

(6) Unaccompanied baggage

The provisions of Baggage Rules are also extended to unaccompanied baggage except where they have been specifically excluded.

- The unaccompanied baggage should be in the possession abroad of the passenger and shall be dispatched within one month of his arrival in India or within such further period as the Deputy/Assistant Commissioner of Customs may allow.
- The unaccompanied baggage may land in India upto two months before the arrival of the passenger or within such period, not exceeding one year as the Deputy/Assistant Commissioner of Customs

may allow, for reasons to be recorded, if he is satisfied that the passenger was prevented from arriving in India within the period of two months due to circumstances beyond his control, such as sudden illness of the passenger or a member of his family, or natural calamities or disturbed conditions or disruption of the transport or travel arrangements in the country or countries concerned on any other reasons, which necessitated a change in the travel schedule of the passenger.

IV. GOODS IMPORTED OR EXPORTED BY POST [SECTION 82 TO 84]

As already stated, Sections 82 to 84 deal with goods imported or exported by post. These provisions are discussed herein below:

(a) Label or Declaration accompanying Goods to be treated as Entry [Section 82]

Section 82 of the Act lays down that in the case of goods imported or exported by post any label or declaration accompanying the goods which contains the description, quantity and value thereof shall be deemed to be an entry for import or export, as the case may be for the purpose of this Act.

(b) Rate of Duty and Tariff Valuation in respect of Goods Imported or Exported by Post [Section 83]

Section 83(1) lays down that the rate of duty and tariff value, if any, applicable to any goods imported by post shall be the rate and valuation in force on the date on which the postal authorities present to the proper officer a list containing the particulars of such goods for the purpose of assessing the duty thereon, provided that if such goods are imported by a vessel and the list of the goods containing the particulars was presented before the date of the arrival of the vessel, it shall be deemed to have been presented on the date of such arrival.

Section 83(2) lays down that the rate of duty and tariff value, if any, applicable to any goods exported by post shall be the rate and valuation in force on the date on which the exporter delivers such goods to the postal authorities for exportation.

(c) Regulations Regarding Goods Imported or to be Exported by Post [Section 84]

The Board may make regulations providing for —

- (a) the form and manner in which an entry may be made in respect of any specified class of goods imported or to be exported by post, other than goods which are accompanied by a label or declaration containing the description, quantity and value thereof.
- (b) the examination, assessment to duty, and clearance of goods imported or to be exported by post.
- (c) the transit or transhipment of goods imported by post from one customs station to another or to a place outside India (Section 84).

V. STORES [SECTION 85 TO 90]

Sections 85 to 90 deal with Stores i.e. goods which are supplied as Stores to the vessels or aircrafts. These provisions are as follows:

(a) Stores may be allowed to be warehoused without assessment to duty [Section 85]

Where any imported goods are entered for warehousing and the importer makes and subscribes to a declaration that the goods are to be supplied as stores to vessels or aircraft without payment of import duty

under this Chapter (i.e. Chapter XI) the proper officer may permit the goods to be warehoused without the goods being assessed to duty (Section 85).

(b) *Transit and Transhipment of Stores [Section 86]*

Any stores imported in a vessel or aircraft may without payment of duty, remain on board such vessel or aircraft while it is in India. [Section 86(1)].

Any stores imported in a vessel or aircraft may with the permission of proper officer be transferred to any vessel or aircraft as stores for consumption therein as provided in Section 87 or Section 90 [Section 86(2)].

In exercise of the powers conferred under Section 86, the Central Board of Revenue has made the Imported Stores (Retention on Board) Regulations, 1963 According to these regulations, any imported stores on board a vessel arriving from a foreign port or an aircraft arriving from a foreign airport may remain on board such vessel or aircraft without payment of import duty leviable thereon during the period such vessel or aircraft is not a foreign-going vessel or aircraft, subject to the condition that where such stores are consumable stores:

- (a) in the case of alcoholic liquor, cigarettes, cigars and pipe tobacco, such stores are kept under Customs seal;
- (b) in the case of consumable stores other than those specified in clause (a) such of other stores are likewise kept under Customs seal.

Provided that if the proper officer is satisfied that it is not practicable so to do, he may, after taking inventory of such stores, allow them to remain on board without being put under Customs seal. Where any stores have been kept under Customs Seal, such seal shall not be broken until the vessel or aircraft becomes a foreign-going vessel or aircraft.

(c) *Imported Stores may be Consumed on Board a Foreign going Vessel or Aircraft [Section 87]*

Any imported stores on board a vessel or aircraft (other than stores to which Section 90 applies) may without payment of duty be consumed thereon as stores during the period such vessel or aircraft is a foreign-going vessel or aircraft. (Section 87).

The Central Board of Excise and Customs has made the Bonded Aircraft Stores (Procedure) Regulations, 1965 which provide for the following:

(d) *Warehousing of goods for use as stores*

- (1) Where any imported goods for use in a foreign-going aircraft are to be entered for warehousing under Section 85 of the Act, an application in Form I shall be made to the Assistant Commissioner of Customs.
- (2) Every such application shall be deemed to be the Bill of Entry in relation to the goods supplied specified in that application for the purpose of Section 46 of the Act.
- (3) On receipt of an application under Sub-regulation (1), the Assistant Commissioner of Customs may permit the goods specified in that application to be warehoused without the goods being assessed to duty.

(e) *Clearance of Warehoused Goods for Supply as Stores in a Foreign going Aircraft*

- (1) Where goods permitted to be warehoused under sub-regulation (3) of regulation 3 (above) are to be cleared for use as stores in a foreign-going aircraft, an application shall be, made to the Assistant Commissioner of Customs in Form II.

- (2) Every such application shall be deemed to be the shipping bill in relation to the goods specified in that application for the purpose of Section 50 of the Act.
- (3) On receipt of an application under Sub-regulation (1) the Assistant Commissioner of Customs may permit the clearance of the warehoused goods specified in that application for being taken on board the foreign-going aircraft as stores in accordance with the provisions of Section 69 of the Act as applied to stores by Section 88 of the said Act.

(f) Application of Section 69 of Chapter X to Stores [Section 88]

Section 88 provides that provisions of Section 69 and Chapter X shall apply to stores (other than those to which Section 90 applies) as they apply to other goods, subject to the modifications that:

- (a) for the words, “exported to any place outside India” or the word “exported” wherever they occur, the words “taken on board any foreign-going vessel or aircraft as stores” shall be substituted.
- (b) in the case of drawback on fuel and lubricating oil taken on board any foreign-going aircraft as stores. Sub-section (1) of Section 74 shall have effect as if for the words “ninety-eight per cent” the words ‘the whole’ were substituted.

(g) Stores to be Free of Export Duty [Section 89]

Goods produced or manufactured in India and required as stores on any foreign-going vessel or aircraft may be exported free of duty in such quantities as the proper officer may determine having regard to the size of the vessel or aircraft, the number of passengers and crew and the length of the voyage or journey on which the vessel or aircraft is about to depart (Section 89).

(h) Concession in respect of imported stores for the Navy [Section 90]

Section 90(1) provides that, imported stores specified in Sub- section (3) may without payment of duty be consumed on board a ship of the Indian Navy.

Section 90(2) lays down that the provisions of Section 69 and Chapter X shall apply to stores specified in Sub-section (3) as they apply to other goods, subject to modification that:

- (a) for the words “exported to any place outside India” or the word “exported” wherever they occur, the words “taken on board a ship of the Navy” shall be substituted.
- (b) for the words, “ninety-eight per cent” in Sub-section (1) of Section 74, the words “the whole” shall be substituted.

The stores referred to in Sub-sections (1) and (2) are the following:

- (a) Stores for the use of a ship of the Indian Navy;
- (b) Stores supplied free by the Government for the use of the crew of a ship of the Indian Navy in accordance with their conditions of service [Section 90(3)].

VI. PROVISIONS RELATING TO COASTAL GOODS AND VESSELS CARRYING COASTAL GOODS [SECTION 91 TO 99]

Chapter XII deals with provisions relating to coastal goods and vessels carrying coastal goods. These provisions do not apply to baggage and stores (Section 91).

The important provisions relating to coastal goods and vessels carrying coastal goods are given below:

(a) Entry of Coastal Goods [Section 92]

The consignor of any coastal goods shall make an entry thereof by presenting to the proper officer a Bill of

Coastal Goods in the prescribed form. [Section 92(1)]. The Bill of Coastal Goods (Form) Regulations, 1976 have prescribed the Form for purposes of this Section.

Every such consignor while presenting a bill of coastal goods shall, at the foot thereof, make and subscribe to a declaration as to the truth of the contents of such bill.

(b) Coastal Goods not to be Loaded until Bill relating thereto is passed [Section 93]

Section 93 lays down that the master of a vessel shall not permit the loading of any Coastal goods on the vessel until a bill relating to such goods presented under Section 92 has been passed by the proper officer and has been delivered to the master by the consignor.

(c) Clearance of Coastal Goods at Destination [Section 94]

Section 94 lays down that the master of a vessel carrying any coastal goods shall carry on board the vessel all bills relating to such goods delivered to him under Section 93 and shall immediately on arrival of the vessel at any customs or coastal port, deliver to the proper officer of the port all bills relating to the goods which are to be unloaded at the port. Section 94(1) provides that where any coastal goods are unloaded at any port, the proper officer shall permit clearance thereof if he is satisfied that they are entered in a bill of coastal goods delivered to him under Sub-section (1).

(d) Master of a coastal vessel to carry an advice book [Section 95]

Section 95 lays down that the master of every vessel carrying coastal goods shall be supplied with a book to be called the advice book. The proper officer at each port of call by such vessel shall make such entries in the advice book as he deems fit, relating to the goods loaded on the vessel at that port. The master of every such vessel shall carry the advice book on board the vessel and shall on arrival at each port of call, deliver it to the proper officer at that port for his inspection.

(e) Loading and Unloading of Coastal Goods at Customs Port or Coastal Port Only [Section 96]

As per Section 96, no coastal goods shall be loaded on, or unloaded from any vessel at any port other than a customs port or a coastal port appointed under Section 7 for the loading of such goods.

(f) No Coastal Vessel to Leave Without Written Order [Section 97]

Section 97 provides that, the master of a vessel which has brought or loaded any coastal goods at a customs port shall not cause or permit the vessel to depart from such port until a written order to that effect has been given by the proper officer.

No such order shall be given until:

- (a) the master of the vessel has answered the question put to him under Section 38;
- (b) all charges and penalties due in respect of that vessel or from the master thereof have been paid or the payment secured by such guarantee or deposit such amount as the proper officer may direct.
- (c) the master of the vessel has satisfied the proper officer that no penalty is leivable on him under Section 116 or the payment of any penalty that may be levied upon him under that section has been secured by such guarantee or deposit of such amount as the proper officer may direct.
- (d) the provisions of this Chapter and any rules and regulations relating to coastal goods and vessels carrying coastal goods have been complied with. [Section 97(2)].

(g) Application of certain provisions of this Act to coastal goods, etc. [Section 98]

Section 98 provides that Sections 33, 34, 36 shall, so far as may be apply to coastal goods as they apply to

imported goods. Sections 37 and 38 shall, so far as may be, apply to vessels carrying coastal goods as they apply to vessels carrying imported goods or export goods.

The Central Government may by notification in the Official Gazette, direct that all or any of the other provisions of Chapter V and provisions of Section 45 shall apply to coastal goods subject to such exceptions and modifications as may be specified in the notification.

(h) Power to make rules in respect of coastal goods and coastal vessels [Section 99]

Section 99 empowers the Central Government to make rules for:

- Preventing the taking out of India of any coastal goods the export of which is dutiable or prohibited under this Act or any other law for the time being in force.
- Preventing in the case of a vessel carrying coastal goods as well as imported or export goods, the substitution of imported or export goods by coastal goods.

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

- Explain the advantages of keeping goods in a warehouse?
- What is warehousing period? Whether any interest is payable on warehoused goods? Discuss.
- What do you understand by the term 'Duty Drawback'?
- What is minimum and maximum drawback under Section 75 of the Customs Act?
- What are the essential elements required for entitlement of 'drawback' on re-export of imported goods?
- What are the rates of Drawback under Section 75 of the Act ?
- Distinguish between duty drawback under sections 74 and 75?
- What is temporary detention of Baggage under Section 80 of the Customs Act?
- What do you mean by stores? When 100% of duty is refunded as a duty drawback on stores?
- What are 'Public' (Bonded) Warehouses and 'Private' (Bonded) Warehouses?
- What are the provisions regarding appointment of Public (Bonded) Warehouses and Licensing of Private (Bonded) Warehouses under the Customs Act, 1962?
- What is the relevant date for rate of duty in case of goods imported or exported by post?

SUGGESTED READINGS

- Customs Law Manual — R. K. Jain
- Indirect Taxes—Law and Practice — V. S. Datey

CUSTOMS LAW

PART V: SEARCH, SEIZURE, CONFISCATION OF GOODS, OFFENCES AND PENALTIES

This part is divided into

- I. Searches, Seizure and Arrest (Section 100 to 110A)
- II. Confiscation of goods and conveyances and imposition of penalties (Section 111 to 127)
- III. Offences and Prosecutions (Section 132 to 140A)

I. SEARCHES, SEIZURE AND ARREST

The Customs Law seeks to regulate imports and exports. It is, therefore, necessary for the customs Department to be fully equipped to meet situations where there is any illegal export or import of goods. In any fiscal enactment, it is common to find provisions relating to searches, seizure and arrest. These provisions only advance the primary objective of the law namely "Prevention of illegal imports and exports. At the same time, it should be remembered that the Customs Act does not aim at detection of a crime. The Customs Officers are also not primarily concerned with the detection and punishment of a crime but they are entrusted in ensuring that there is no smuggling of contraband articles. They have to safeguard the recovery of customs duty properly applicable to the goods. Chapter XIII of the Act consisting of Sections 100 to 110A contains detailed provisions in regard to searches, seizure and arrest. These are discussed below:

(A) POWER TO SEARCH SUSPECTED PERSONS ENTERING OR LEAVING INDIA(SECTION 100)

Under Section 100 of the Act where the proper officer of the Customs has reason to believe that the following categories of persons have secreted any goods, liable to confiscation or any documents thereto, he may search such persons.

The categories of persons referred to in the above paragraph are: -

- (a) any person who has landed from or is about to board, or is on board any vessel within the Indian Customs waters;
- (b) any person who has landed from or is about to board, or is on board a foreign-going aircraft;
- (c) any person who has got out of, or is about to get into, or is in vehicle, which has arrived from, or is to proceed to any place outside India;
- (d) any person not included in clauses (a), (b) or (c) who has entered or is about to leave India;
- (e) any person in a customs area.

(B) POWER TO SEARCH SUSPECTED PERSONS IN CERTAIN OTHER CASES (SECTION 101)

Under Section 101 of the Act, an officer of the Customs empowered generally or specially by an order of Commissioner of Customs can search any person if he has reason to believe that any person has secreted about his person, the following goods which are liable to confiscation, or documents relating thereto:

- (a) gold;
- (b) diamonds;

- (c) manufactures of gold or diamond;
- (d) watches;
- (e) any other class of goods which the Central Government may, by notification in the Official Gazette, specify.

The power under Section 101 is without prejudice to the power conferred under Section 100 of the Act. Again under Section 101 any person can be searched.

(C) PERSONS TO BE SEARCHED MAY REQUIRE TO BE TAKEN BEFORE GAZETTED OFFICER OF CUSTOMS OR MAGISTRATE (SECTION 102)

Section 102 of the Act provides that when any officer of Customs is about to search any person in terms of Sections 100 and 101, he shall, if such person so requires, take him without unnecessary delay to the nearest Gazetted Officer of customs or magistrate. If such requisition is made, the officer of customs may detain the person making it until, he can bring him before the gazetted officer of customs or the magistrate. The Gazetted Officer of customs or the magistrate before whom any "such person is brought shall, if he sees no reasonable ground for search, forthwith discharge the person. In other cases, he shall direct that a search be made. Before making a search, the officer of Customs shall call upon two or more persons to attend and witness the search and may issue an order in writing to them or any of them so to do. The search would be made in the presence of such persons and a list of all things seized in the course of such search shall be prepared by such officer or other person and signed by such witnesses. Where the person to be searched is a female, the search shall be done only by a female.

(D) POWER TO SCREEN OR X-RAY BODIES OF SUSPECTED PERSONS FOR DETECTING SECRETED GOODS (SECTION 103)

Section 103 of the Act contains powers, to screen or X-Ray bodies of persons suspected of secreting certain goods liable to confiscation. Under this section, detention of a person and production without unnecessary delay before the nearest Magistrate by the proper officer is envisaged. The Magistrate before whom any person is brought shall, if he sees how reasonable ground for believing that such person has any such goods secreted inside his body, forthwith discharge such person. On the other hand, where the Magistrate has reasonable ground for believing that any such person has any such goods liable for confiscation secreted in his body and the Magistrate is satisfied that an X-Ray is necessary for this purpose, he may make an order to a radiologist possessing qualifications recognised by the Central Government for the purpose of screening or X-raying the body of any person, such person would be taken to a radiologist for the purpose of screening or X-raying the body. The radiologist shall, after the screening or X-Ray, forward his report together with the X-Ray picture taken by him to the Magistrate without unnecessary delay. On receipt of the report of radiologist, if the Magistrate is satisfied that any person has any goods liable to confiscation secreted inside his body, he may direct; that suitable action for bringing out such goods be taken on the advice and under the supervision of a registered medical practitioner and such person shall be bound to comply with such direction. In the case of a female, the advice and supervision of a female registered medical practitioner is required. For the purposes of complying with the provisions of this section any person brought before the Magistrate may be detained by him for such period as the Magistrate may direct.

The above provisions will not apply to any such person who admits that goods liable to confiscation are secreted in his body and who voluntarily submits himself for suitable action being taken for bringing out such goods.

(E) POWER TO ARREST (SECTION 104)

If an officer of customs empowered in this behalf by general or special order of the Commissioner of

Customs has reason to believe that any person in India or within the Indian customs waters has committed an offence punishable under section 132 or section 133 or section 135 or section 135A or section 136, he may arrest such person and shall, as soon as may be, inform him of the grounds for such arrest [Section 104(1)].

Every person arrested shall, without unnecessary delay, be taken to a magistrate (Sub-section 2 of Section 104)

Where an officer of customs has arrested any person he shall, for the purpose of releasing such person on bail or otherwise, have the same powers and be subject to the same provisions as the officer-in-charge of a police station has and is subject to under the Code of Criminal Procedure, 1898.

As per sub-section (4), notwithstanding anything contained in the Code of Criminal Procedure, 1973, any offence relating to--

- (a) prohibited goods; or
- (b) evasion or attempted evasion of duty exceeding Rs. 50 Lakh, shall be cognizable.

All other offences under the Act shall be non-cognizable except the two above.

As per sub-section (6), notwithstanding anything contained in the Code of Criminal Procedure, 1973 (2 of 1974), an offence punishable under section 135 relating to -

- (a) evasion or attempted evasion of duty exceeding fifty lakh rupees; or
- (b) prohibited goods notified under section 11 which are also notified under sub-clause (C) of clause (i) of sub-section (1) of section 135; or
- (c) import or export of any goods which have not been declared in accordance with the provisions of this Act and the market price of which exceeds one crore rupees; or
- (d) fraudulently availing of or attempt to avail of drawback or any exemption from duty provided under this Act, if the amount of drawback or exemption from duty exceeds fifty lakh rupees, shall be non-bailable.

Except as provided in sub section (6), all other offences under this Act shall be bailable.

POWER TO SEARCH PREMISES (SECTION 105)

Section 105 of the Act deals with it. The Assistant/Deputy Commissioner of Customs or any other officer of customs in case of any area adjoining the land frontier or the coast of India specially empowered by name in this behalf by the Board, if he has reason to believe that any goods liable to confiscation or any documents or things which in his opinion will be useful to any proceedings under the Act, are secreted in any place, he may authorise any officer of customs to search or may himself search for such goods, documents, or things. For the purposes of conducting such a search, the provisions of the Code of Criminal Procedure, 1973 relating to searches would apply.

POWER TO STOP AND SEARCH CONVEYANCES (SECTION 106)

Section 106 of the Act deals with it. Accordingly, where the proper officer has reason to believe that any aircraft, vehicle or animal in India or any vessel in India or within the Indian customs waters has been, is being, or is about to be, used in the smuggling of any goods or in the carriage of any goods which have been smuggled, he may at any time stop any such vehicle, animal or vessel or, in the case of an aircraft, compel it to land, and

- (a) rummage and search any part of the aircraft, vehicle or vessel;

- (b) examine and search any goods in the aircraft, vehicle or vessel or on the animal;
 - (c) break open the lock of any door or package for exercising the powers conferred by clauses (a) and (b), if the keys are withheld.
- (2) Where for the above purpose—
- (a) it becomes necessary to stop any vessel or compel any aircraft to land, it shall be lawful for any vessel or aircraft in the service of the Government while flying her proper flag and any authority authorised in this behalf by the Central Government to summon such vessel to stop or the aircraft to land, by means of an international signal, code or other recognised means, and thereupon such vessel shall forthwith stop or such aircraft shall forthwith land; and if it fails to do so, chase may be given thereto by any vessel or aircraft as aforesaid and if after a gun is fired as a signal the vessel fails to stop or the aircraft fails to land, it may be fired upon;
 - (b) it becomes necessary to stop any vehicle or animal, the proper officer may use all lawful means for stopping it, and where such means fail, the vehicle or animal may be fired upon.

POWER TO INSPECT (SECTION 106A)

Section 106A of the Act empowers an Officer of Customs to enter any place intimated under Chapter IVA or IVB of the Act and inspect the goods kept or stored therein and require any person found therein, who is for the time being in charge thereof, to produce to him for this inspection the accounts maintained under the said Chapter IVA or Chapter IVB and to furnish to him such other information as he may reasonably require for the purpose of ascertaining whether or not such goods have been illegally imported, exported or likely to be illegally exported.

POWER TO EXAMINE PERSONS (SECTION 107)

Under Section 107 of the Act, any Officer of Customs empowered specially or generally by an order of the Commissioner of Customs may, during the course of any enquiry in connection with the smuggling of any goods—

- (a) require any person to produce or deliver any document or thing relevant to the enquiry;
- (b) examine any person acquainted with the facts and circumstances of the case.

POWER TO SUMMON PERSONS TO GIVE EVIDENCE AND PRODUCE DOCUMENTS (SECTION 108)

Section 108 of the Act deals with it. Accordingly, any Gazetted Officer of customs duty (the words “empowered by the Central Government”, has been omitted by Finance Act, 2008 w.e.f. 13th July 2006) shall have power to summon any person whose attendance he considers necessary either to give evidence or to produce a document or any other thing in any inquiry which such officer is making in connection with the smuggling of any goods.

A summons to produce documents or other things may be for the production of certain specified documents or things or for the production of all documents or things of a certain description in the possession or under the control of the person summoned.

All persons so summoned shall be bound to attend either in person or by an authorised agent, as such officer may direct; and all persons so summoned shall be bound to state the truth upon any subject respecting which they are examined or make statements and produce such documents and other things as may be required.

Provided that the exemption under Section 132 of the Code of Civil Procedure, 1908 (5 of 1908), shall be applicable to any requisition for attendance under this section.

Every such inquiry as aforesaid shall be deemed to be a judicial proceeding within the meaning of Section 193 and Section 228 of the Indian Penal Code, 1860 (45 of 1860).

POWER TO REQUIRE PRODUCTION OF ORDER PERMITTING CLEARANCE OF GOODS IMPORTED BY LAND (SECTION 109)

Under Section 109 of the Act, any Officer of Customs appointed for any area adjoining the land frontier of India and "empowered generally or specially by an order by the Board, may require any person in possession of any goods which such officer has reason to believe to have been imported into India by land, to produce the order made under Section 47 permitting clearance of the goods. The provisions of this section shall not apply to any imported goods passing from a land frontier to a land customs station by a route appointed under clause (c) of Section 7.

SEIZURE OF GOODS, DOCUMENTS AND THINGS (SECTION 110)

Under Section 110 of the Act, if the proper officer of Customs has reason to believe that any goods are liable to confiscation under the Act, he may seize such goods. Where it is not practicable to seize such goods, the proper officer may serve on the owner of the goods an order that he shall not remove, part with, or otherwise deal with the goods except with the previous permission of such officer.

The Central Government may, having regard to the perishable or hazardous nature of any goods, depreciation in the value of the goods with the passage of time, constraints of storage space for the goods or any other relevant considerations, by notification in the Official Gazette, specify the goods or class of goods which shall, as soon as may be, after its seizure under Sub-section (1), be disposed of by the proper officer in such manner as the Central Government may, from time to time, determine after following the procedure hereinafter specified.

In exercise of the powers conferred by Sub-section (1A) of Section 110 of the Customs Act, 1962 (52 of 1962), the Central Government, having regard to the perishable nature, depreciation in the value with the passage of time, constraints of storage space and valuable nature of the goods, has specified the following goods, namely:

1. Liquors;
2. Primary cells and primary batteries including re-chargeable batteries;
3. Wrist watches including electronic wrist watches; watch movements or components thereof;
4. All electronic goods including television sets, video cassette recorders, tape recorders, calculators, computers; components and spares thereof including diodes, transistors, integrated circuits etc; and
5. Dangerous drugs and psychotropic substances."

Where any goods, being goods specified above have been seized by a proper officer under Sub-section (1), he shall prepare an inventory of such goods containing such details relating to their description, quality, quantity, mark, numbers, country of origin and other particulars as the proper officer may consider relevant to the identity of the goods in any proceedings under this Act and shall make an application to a Magistrate for the purpose of —

- (a) certifying the correctness of the inventory so prepared; or
- (b) taking, in the presence of the Magistrate, photographs of such goods and certifying such

photographs as true; or

- (c) allowing to draw representative samples of such goods, in the presence of the Magistrate, and certifying the correctness of any list of samples so drawn.

Where any application is made as above, the Magistrate, shall allow the application.

Where any goods are seized and no notice in respect thereof is given under clause (a) of Section 124 within 6 months of seizure of the goods, the goods shall be returned to the person from whose possession they were seized. This period of 6 months however, can be extended by the Commissioner of Customs for a period not exceeding six months.

The proper officer may seize any documents or things which in his opinion, will be useful for, or relevant to, any proceeding under this Act. The person from whose custody any documents are seized is entitled to make copies thereof or take extracts therefrom in the presence of an officer of customs.

Provisional Release of goods, document and things seized pending Adjudication (Section 110A)

Any goods, documents or things seized under Section 110 may, pending the order of the adjudicating authority, be released to the owner on taking a bond from him in the proper form with such security and conditions as the adjudicating authority may require.

PART II: CONFISCATION OF GOODS (SECTION 111 TO 127)

Goods become liable to confiscation if the Importer or Exporter contravenes any of the provisions of the Customs Act, 1962 or any other Act for the time being in force in relation to the importation and exportation of goods. Some of the more important allied statutes that get attracted in this manner are, to mention just a few, the Arms Act, the Copyright Act, the Dangerous Drugs Act, the Foreign Exchange Management Act, the Imports and Exports (Control) Act, the Trade Marks Act and the Ancient Monuments Preservation Act. The responsibility of the Officers of Customs to ensure that none of the provisions of these and such enactments is contravened, is thus onerous. It is also to meet that there are several instances of contraventions of these provisions and this has paved the way to procedures being laid down for, not only bringing the contraventions to the notice of those concerned, but also to take those responsible to task for non-compliance with statutory obligations. Of course, there are contraventions of the Customs Act, 1962 also and all these are taken care of by the set procedures for adjudication.

We have already seen that Section 28 of the Customs Act provides for a notice to be issued to the Importer or Exporter of any goods if duties of Customs have not been levied or have been short levied or erroneously refunded. Similarly, if any contravention of any provision of any Act for the time being in force is noticed, it is a statutory obligation placed on the Department that a notice of show cause be issued to the person concerned, so that he is given an opportunity to explain his side of the matter. Section 124 of the Customs Act lays down as follows:

(A) CONFISCATION OF IMPROPERLY IMPORTED GOODS ETC. (SECTION 111)

Under Section 111, the following goods brought from a place outside India shall be liable to confiscation: -

- (a) any goods imported by sea or air which are unloaded or attempted to be unloaded at any place other than a customs port or customs airport appointed under clause (a) of Section 7 for the unloading of such goods;
- (b) any goods imported by land or inland water through any route other than a route specified in a notification issued under clause (c) of Section 7 for the import of such goods;

- (c) any dutiable or prohibited goods brought into any bay, gulf, creek or tidal river for the purpose of being landed at a place other than a customs port;
- (d) any goods which are imported or attempted to be imported or are brought within the Indian customs waters for the purpose of being imported, contrary to any prohibition imposed by or under this Act or any other law for the time being in force;
- (e) any dutiable or prohibited goods found concealed in any manner in any conveyance;
- (f) any dutiable or prohibited goods required to be mentioned under the regulations in an import manifest or import report which are not so mentioned;
- (g) any dutiable or prohibited goods which are unloaded from a conveyance in contravention of the provisions of Section 32, other than goods inadvertently unloaded but included in the record kept under Sub-section (2) of Section 45;
- (h) any dutiable or prohibited goods unloaded or attempted to be unloaded in contravention of the provisions of Section 33 or Section 34;
- (i) any dutiable or prohibited goods found concealed in any manner in any package either before or after the unloading thereof;
- (j) any dutiable or prohibited goods removed or attempted to be removed from a customs area or a warehouse without the permission of the proper officer or contrary to the terms of such permission;
- (k) any dutiable or prohibited goods imported by land in respect of which the order permitting clearance of the goods required to be produced under Section 109 is not produced or which do not correspond in any material particular with the specification contained therein;
- (l) any dutiable or prohibited goods which are not included or are in excess of those included in the entry made under this Act, or in the case of baggage in the declaration made under Section 77;
- (m) any goods which do not correspond in respect of value or in any other particular with the entry made under this Act or in the case of baggage with the declaration made under Section 77 in respect thereof, or in the case of goods under transhipment, with the declaration for transhipment referred to in the proviso to Sub-section (1) of Section 54.
- (n) any dutiable or prohibited goods transited with or without transhipment or attempted to be so transited in contravention of the provisions of Chapter VIII;
- (o) any goods exempted, subject to any condition, from duty or any prohibition in respect of the import thereof under this Act or any other law for the time being in force, in respect of which the condition is not observed, unless the non-observance of the condition was sanctioned by the proper officer;
- (p) any notified goods in relation to which any provisions of Chapter IVA or of any rule made under this Act for carrying out the purposes of that Chapter have been contravened.

PENALTY FOR IMPROPER IMPORTATION OF GOODS, ETC. (SECTION 112)

Under Section 112, any person:

- (a) who, in relation to any goods, does or omits to do any act which act or omission would render such goods liable to confiscation under Section 111, or abets the doing or omission of such an act, or
- (b) who acquires possession of or is in any way concerned in carrying, removing, depositing, harbouring, keeping, concealing, selling or purchasing, or in any other manner dealing with any goods which he knows or has reason to believe are liable to confiscation under Section 111;

shall be liable:

- (i) in the case of goods in respect of which any prohibition is in force under this Act or any other law for the time being in force, to a penalty not exceeding the value of the goods or five thousand rupees, whichever is the greater;
- (ii) in the case of dutiable goods, other than prohibited goods, to a penalty not exceeding the duty sought to be evaded on such goods or five thousand rupees, whichever is the greater;
- (iii) in the case of goods in respect of which the value stated in the entry made under this Act or in the case of baggage, in the declaration made under Section 77 (in either case hereafter in this section referred to as the declared value) is higher than the value thereof, to a penalty not exceeding the difference between the declared value and the value thereof or five thousand rupees, whichever is the greater;
- (iv) in the case of goods falling both under clauses (i) and (ii), to a penalty not exceeding the value of the goods or the difference between the declared value and the value thereof or five thousand rupees, whichever is the highest;
- (v) in the case of goods falling both under clauses (ii) and (iii), to a penalty not exceeding the duty sought to be evaded on such goods or five times the difference between the declared value and the value thereof or five thousand rupees, whichever is the highest.

CONFISCATION OF GOODS ATTEMPTED TO BE IMPROPERLY EXPORTED, ETC. (SECTION 113)

The following export goods shall be liable to confiscation, under Section 113 of the Act:

- (a) any goods attempted to be exported by sea or air from any place other than a customs port or a customs airport appointed for the loading of such goods;
- (b) any goods attempted to be exported by land or inland water through any route other than a route specified in a notification issued under clause (c) of Section 7 for the export of such goods;
- (c) any goods brought near the land frontier or the coast of India or near any bay, gulf, creek or tidal river for the purpose of being exported from a place other than a land customs station or a customs port appointed for the loading of such goods;
- (d) any goods attempted to be exported or brought within the limits of any customs area for the purpose of being exported, contrary to any prohibition imposed by or under this Act or any other law for the time being in force;
- (e) any goods found concealed in a package which is brought within the limits of a customs area for the purpose of exportation;
- (f) any goods which are loaded or attempted to be loaded in contravention of the provisions of Section 33 or Section 34;
- (g) any goods loaded or attempted to be loaded on any conveyance, or water-borne, or attempted to be water-borne for being loaded on any vessel, the eventual destination of which is a place outside India, without the permission of the proper officer;
- (h) any goods which are not included or are in excess of those included in the entry made under this Act, or in the case of baggage in the declaration made under Section 77;
- (i) any goods entered for exportation which do not correspond in respect of value or in any material particular with the entry made under this Act or in the case of baggage with the declaration made under Section 77;

- (j) any goods entered for exportation under claim for drawback which do not correspond in any material particular with any information furnished by the exporter or manufacturer under this Act in relation to the fixation of rate of drawback under Section 75.
- (k) any goods on which import duty has not been paid and which are entered for exportation under Section 74;
- (l) any goods cleared for exportation under a claim for drawback which are not loaded for exportation on account of any wilful act, negligence or default of the exporter, his agent or employee, or which after having been loaded for exportation are unloaded without the permission of the proper officer;
- (m) any specified goods in relation to which any provisions of Chapter IVB or of any rule made under this Act for carrying out the purposes of that Chapter have been contravened.

PENALTY FOR ATTEMPT TO EXPORT GOODS IMPROPERLY ETC. (SECTION 114)

According to Section 114 any person who, in relation to any goods, does or omits to do, any act, which act or omission would render such goods liable to confiscation under Section 113, or abet the doing or omission of such an act, shall be liable:

- (i) in the case of goods in respect of which any prohibition is in force under this Act or any other law for the time being in force, to a penalty not exceeding three times the value of the goods as declared by the exporter or the value as determined under this Act, whichever is the greater;
- (ii) in the case of dutiable goods, other than prohibited goods, to a penalty not exceeding the duty sought to be evaded or five thousand rupees, whichever is the greater;
- (iii) in the case of any other goods, to a penalty not exceeding the value of the goods, as declared by the exporter or the value as determined under this Act, whichever is greater.

PENALTY FOR SHORT-LEVY OR NON-LEVY OF DUTY IN CERTAIN CASES (SECTION 114A)

Section 114A inserted by the Finance (No. 2) Act, 1996 w.e.f. 28.9.96, prescribes a mandatory penalty equal to the duty or interest not levied, short levied, not paid or part paid or erroneously refunded by reason of collusion or willful mis-statement or suppression of facts by the person liable to pay the duty. The section reads as under—

Where the duty has not been levied or has been short-levied or the interest has not been charged or paid or has not been part paid or the duty or interest has been erroneously refunded by reason of collusion or any wilful mis-statement or suppression of facts, the person who is liable to pay the duty or interest, as the case may be, as determined under Sub-section (2) of Section 28 shall also be liable to pay a penalty equal to the duty or interest so determined:

Provided that where such duty or interest, as the case may be, as determined under Sub-section (2) of Section 28, and the interest payable thereon under Section 28AB, is paid within thirty days from the date of the communication of the order of the proper officer determining such duty, the amount of penalty liable to be paid by such person under this section shall be twenty-five per cent of the duty or interest, as the case may be, so determined:

Provided further that the benefit of reduced penalty under the first proviso shall be available subject to the condition that the amount of penalty so determined has also been paid within the period of thirty days referred to in that proviso:

Provided also that where the duty or interest determined to be payable is reduced or increased by the

Commissioner (Appeals), the Appellate Tribunal or, as the case may be, the court, then, for the purposes of this section, the duty or interest as reduced or increased, as the case may be, shall be taken into account.

Provided also that in case where the duty or interest determined to be payable is increased by the Commissioner (Appeal), the Appellate Tribunal or, as the case may be, the court, then, the benefit of reduced penalty under the first proviso shall be available if the amount of the duty or the interest so increased, along with the interest payable thereon under Section 28AB, and twenty-five per cent of the consequential increase in penalty have also been paid within thirty days of the communication of the order by which such increase in the duty or interest takes effect:

Provided also that where any penalty has been levied under this section, no penalty shall be levied under Section 112 or Section 114.

Explanation — For the removal of doubts, it is hereby declared that:

- (i) the provisions of this section shall also apply to cases in which the order determining the duty or interest under Sub-section (2) of Section 28 relates to notices issued prior to the date on which the Finance Act, 2000 receives the assent of the President;
- (ii) any amount paid to the credit of the Central Government prior to the date of communication of the order referred to in the first proviso or the fourth proviso shall be adjusted against the total amount due from such person.

PENALTY FOR USE OF FALSE AND INCORRECT MATERIAL (SECTION 114AA)

Section 114AA provides that if a person knowingly or intentionally makes, signs or uses, or causes to be made, signed or used, any declaration, statement or document which is false or incorrect in any material particular, in the transaction of any business for the purposes of this Act, shall be liable to a penalty not exceeding five times the value of goods.

CONFISCATION OF CONVEYANCES (SECTION 115)

(1) The following conveyances shall be liable to confiscation, under Section 115:

- (a) any vessel which is or has been within the Indian customs waters, any aircraft which is or has been in India, or any vehicle which is or has been in a customs area, while constructed, adapted, altered or fitted in any manner for the purpose of concealing goods;
- (b) any conveyance from which the whole or any part of the goods is thrown overboard, staved or destroyed so as to prevent seizure by an officer of customs;
- (c) any conveyance which having been required to stop or land under Section 106 fails to do so, except for good and sufficient cause;
- (d) any conveyance from which any warehoused goods cleared for exportation, or any other goods cleared for exportation under a claim for drawback, are unloaded, without the permission of the proper officer;
- (e) any conveyance carrying imported goods which has entered India and is afterwards found with the whole or substantial portion of such goods missing, unless the master of the vessel or aircraft is able to account for the loss of, or deficiency in, the goods.

(2) Any conveyance or animal used as a means of transport in the smuggling of any goods or in the carriage of any smuggled goods shall be liable to confiscation, unless the owner of the conveyance or animal proves that it was so used without the knowledge or connivance of the owner himself, his agent, if any, and the person in charge of the conveyance or animal.

Provided that where any such conveyance is used for the carriage of goods or passengers for hire, the owner of any conveyance shall be given an option to pay in lieu of the confiscation of the conveyance a fine not exceeding the market price of the goods which are sought to be smuggled or the smuggled goods, as the case may be.

“Market price” in this section, means market price at the date when the goods are seized. (Explanation added to the section).

PENALTY FOR NOT ACCOUNTING FOR GOODS (SECTION 116)

Under Section 116, if any goods loaded in a conveyance for importation into India, or any goods transhipped under the provisions of this Act or coastal goods carried in a conveyance, are not unloaded at their place of destination in India, or if the quantity unloaded is short of the quantity to be unloaded at that destination, and if the failure to unload or the deficiency is not accounted for to the satisfaction of the Assistant or Deputy Commissioner of Customs, the person-in-charge of the conveyance shall be liable:

- (a) in the case of goods loaded in a conveyance for importation into India or goods transhipped under the provisions of this Act, to a penalty not exceeding twice the amount of duty that would have been chargeable on the goods not unloaded or the deficient goods, as the case may be, had such goods been imported;
- (b) in the case of coastal goods, to a penalty not exceeding twice the amount of export duty that would have been chargeable on the goods not unloaded or the deficient goods, as the case may be, had such goods been exported.

PENALTIES FOR CONTRAVENTION, ETC., NOT EXPRESSLY MENTIONED (SECTION 117)

Any person who contravenes any provision of this Act or abets any such contravention or who fails to comply with any provisions of this Act, with which it was his duty to comply, where no express penalty is elsewhere provided for such contravention or failure, shall be liable to a penalty not exceeding one lakh rupees (Section 117).

CONFISCATION OF PACKAGES AND THEIR CONTENTS (SECTION 118)

- (a) Where any goods imported in a package are liable to confiscation, the package and any other goods imported in that package shall also be liable to confiscation.
- (b) Where any goods are brought in a package within the limits of a customs area for the purpose of exportation and are liable to confiscation, the package and any other goods contained therein shall also be liable to confiscation (Section 118).

CONFISCATION OF GOODS USED FOR CONCEALING SMUGGLED GOODS (SECTION 119)

Any goods used for concealing smuggled goods shall also be liable to confiscation, in terms of Section 119.

“Goods” does not include a conveyance used as a means of transport.

CONFISCATION OF SMUGGLED GOODS NOTWITHSTANDING ANY CHANGE IN FORM, ETC. (SECTION 120)

- (1) Smuggled goods may be confiscated notwithstanding any change in their form.
- (2) Where smuggled goods are mixed with other goods in such manner that the smuggled goods cannot be separated from such other goods, the whole of the goods shall be liable to confiscation.

Provided that where the owner of such goods proves that he had no knowledge or reason to believe that they included any smuggled goods, only such part of the goods the value of which is equal to the value of the smuggled goods shall be liable to confiscation (Section 120).

CONFISCATION OF SALE-PROCEEDS OF SMUGGLED GOODS (SECTION 121)

Where any smuggled goods are sold by a person having knowledge or reason to believe that the goods are smuggled goods, the sale-proceeds thereof shall be liable to confiscation (Section 121).

ADJUDICATION OF CONFISCATIONS AND PENALTIES (SECTION 122)

Section 122 provides that in every case in which anything is liable to confiscation or any person is liable to a penalty, such confiscation or penalty may be adjudged:

- (a) without limit, by a Commissioner of Customs or a Joint Commissioner of Customs;
- (b) where the value of the goods liable to confiscation does not exceed two lakh rupees, by an Assistant or Deputy Commissioner of Customs;
- (c) where the value of the goods liable to confiscation does not exceed ten thousand rupees, by a Gazetted Officer of customs lower in rank than an Assistant or Deputy Commissioner of Customs.

ADJUDICATION PROCEDURE SECTION 122A

The adjudicating authority shall, in any proceeding under this Chapter or any other provision of this Act, give an opportunity of being heard to a party in a proceeding, if the party so desires.

The adjudicating authority may, if sufficient cause is shown at any stage of proceeding, grant time, from time to time, to the parties or any of them and adjourn the hearing for reasons to be recorded in writing:

However, no such adjournment shall be granted more than three times to a party during the proceeding.

BURDEN OF PROOF IN CERTAIN CASES (SECTION 123)

Section 123(1), provides that where any goods to which this section applies are seized under this Act in the reasonable belief that they are smuggled goods, the burden of proving that they are not smuggled goods shall be:

- (a) in a case where such seizure is made from the possession of any person:
 - (i) on the person from whose possession the goods were seized; and
 - (ii) if any person, other than the person from whose possession the goods were seized, claims to be the owner thereof, also on such other person;
- (b) in any other case, on the person, if any, who claims to be the owner of the goods so seized.

Section 123 shall apply to gold and manufactures of watches and any other class of goods which the Central Government may by notification in the Official Gazette specify.

The Central Government has notified the following other classes of goods, for the purposes of Section 123(2), namely:

1. Cosmetics.
2. Cigarettes.
3. Transistors and Diodes.
4. Synthetic yarn and Metallised yarn.

5. Fabrics made wholly or mainly of synthetic yarn.
6. Cassette Tape Recorders.
7. Electronic Calculators.
8. Whisky.
9. Watches, watch movements (including partly assembled movements), dials and cases for watches.
10. Zip fasteners.
11. Video Cassette Recorders and Video Cassette Players.
12. T.V. Sets.

ISSUE OF SHOW CAUSE NOTICE BEFORE CONFISCATION OF GOODS ETC. (SECTION 124)

Section 124, provides that, no order confiscating any goods or imposing any penalty on any person shall be made under this Chapter unless the owner of the goods or such person:

- (a) is given a notice in writing informing him of the grounds on which it is proposed to confiscate the goods or impose a penalty;
- (b) is given an opportunity of making a representation in writing within such reasonable time as may be specified in the notice against the grounds of confiscation or imposition of penalty mentioned therein; and
- (c) is given a reasonable opportunity of being heard in the matter;

Provided that the notice referred to in clause (a) and the representation referred to in clause (b) may, at the request of the person concerned, be oral.

This provision has been made to make it obligatory on the part of adjudicating officers to follow the principles of natural justice. Any order of confiscation or any order imposing a penalty on any person without giving him an opportunity as laid down in Section 124 becomes void and is set aside in a court of law, as can be seen from the following decrees:

"The Commissioner of Central Excise should see that every show cause notice issued under the provisions of the Act strictly complies with, not only the letter of the law, but also the spirit of it (AIR 1962 MAD. 366 at p. 368). The Department is not absolved of the obligation under Section 124 for issuing a show cause notice before passing an order confiscating any goods or imposing any penalty on any person under Chapter XIV of the Customs Act (AIR 1972 GUJ. 115). The object of the show cause notice is not to merely mention the statutory provisions under which the person to whom the notice is issued is liable to be punished by the imposition of penalty; the real object of such a notice is to indicate, besides the nature of the contravention which is sought to be punished under any provision of the Act, the penalty also that is sought to be imposed on the petitioner (AIR 1962 MAD. 366 at p. 368).

OPTION TO PAY FINE IN LIEU OF CONFISCATION (SECTION 125)

Under Section 125 whenever confiscation of goods is authorised by this Act, the officer adjudicating it may, in the case of any goods, the importation or exportation whereof is prohibited under this Act or any other law for the time being in force, and shall, in the case of any other goods, give to the owner of the goods, or where such owner is not known, the person from whose possession or custody such goods have been seized, an option to pay in lieu of confiscation such fine as the said officer thinks fit:

Provided that, without prejudice to the provisions of the proviso to Sub-section (2) of Section 115, such fine shall not exceed the market price of the goods confiscated, less in the case of imported goods, the duty chargeable thereon.

Where any fine in lieu of confiscation of goods is imposed the owner of such goods or the other person shall, in addition, be liable to any duty and charges payable in respect of such goods.

ON CONFISCATION PROPERTY TO VEST IN CENTRAL GOVERNMENT (SECTION 126)

- (1) When any goods are confiscated under this Act, such goods shall thereupon vest in the Central Government.
- (2) The officer adjudicating the confiscation shall take and hold possession of the confiscated goods (Section 126).

AWARD OF CONFISCATION OR PENALTY BY CUSTOMS OFFICERS NOT TO INTERFERE WITH OTHER PUNISHMENTS (SECTION 127)

The award of any confiscation or penalty under this Act by an officer of Customs shall not prevent the infliction of any punishment to which the person affected thereby is liable under the provisions of Chapter XVI or under any other law (Section 127).

Some important case laws relating to adjudication are given herein below to highlight the parameters within which the adjudicating officer has to function:-

- (a) In revision application of M/s. Bijee Products (India) Pvt. Ltd., the Government of India observed: "The lower authorities have not gone into the merits of the refund claim nor have they examined whether the claim was within the time limit specified under the Rules. Government of India, accordingly, set aside the order of the Appellate Collector since it is not a speaking order and direct the Appellate Collector to consider the appeal de-novo now and pass an order on merits" - (1982 ELT 591).
- (b) "If a personal hearing was not given to the petitioner at the adjudication/appellate stage in spite of a specific request made by him in reply to the show cause notice, the adjudication order is not sustainable in law.The revision application disposed of without giving a speaking order is also invalid.If the basic order is invalid, the remaining appellate/ revisionary orders will also be ineffective". - [1982 ELT 350 (P&H)].
- (c) "If the Collector has disposed of the case in a summary fashion without giving due consideration to the points urged by the Appellants and passing a speaking order dealing with them, the case is fit for remand for de-novo trial." - (1982 ELT 436 CBEC).
- (d) "The Assistant Collector (Adjudicating Officer) has no power under law to modify his earlier order or to issue a corrigendum, for Section 154 of the Customs Act only provides for the correction of clerical or arithmetical mistakes or any error or errors arising from accidental slip or omission. As such, the corrigendum issued by the Assistant Collector was without authority." - [1986 (9) ECR 231 - CEGAT].
- (e) "The Assistant Collector, who has given his decision on the 1st February, 1962 has not taken any of these factors into consideration nor has he taken into consideration any of the other evidence offered by the petitioners for deciding this point. Under the circumstances, we find that the decision given by the Assistant Collector, is a result of total non-application of his mind. The same can be said with greater force with regard to the order which the Collector has passed in appeal against the

above order. Whatever be the reasons for the Collector to delay his order for months after the appeal was heard, we find that after this long deliberation over the merits of the appeal, the only order which is recorded is: 'I have examined the facts and merits of the case. I have carefully considered the pleas advanced by the appellants in the appeal petition as also the arguments at the time of personal hearing on 26.12.64. I, however, see no reason to interfere with the decision taken by the Assistant Collector ... in his order ... dated 2.2.63. I uphold the said order and consequently, the appeal is rejected.' It is too obvious to mention that this order cannot be considered as a speaking order. It does not reveal what the facts are that the Collector took into consideration before coming to his conclusion. Under the circumstances, the order suffers from the same infirmity as the order passed by the Assistant Collector does". - (1983 ELT 744 GUJ).

- (f) "It is well established that it is not a good return to a rule nisi for the issue of a writ certiorari to state that the order is justified on facts not contained in the order. This court cannot take cognizance of any fact which does not appear upon the face of the order. When a statutory functionary makes an order based on certain grounds, its validity must be judged by the reasons so mentioned and cannot be supplemented by fresh reasons in the shape of affidavit or otherwise. Otherwise, an order, bad in the beginning may, by the time it comes to court on account of a challenge, get validated by additional grounds later brought out. This ground is not mentioned in the impugned order". - 1984 (15) ELT 379 (MAD).
- (g) ".... In this connection, I may state that the Assistant Collector is a quasi-judicial authority and has to discharge his duties and functions in a quasi-judicial manner. I would like to impress upon the Assistant Collector that he is not bound by any administrative instructions. The questions of fact and law which may be raised before him by the parties are required to be determined by him after full application of mind in an objective manner without feeling in any way controlled by any administrative instructions and he will deal with clearly and expressly the reasonings which may be advanced on behalf of the petitioners. It is only when the petitioners' reasoning is dealt with that it would show that there has been application of mind by him. The above observations have been made in view of the fact that administrative instructions have been brought to my notice by the counsel for the petitioners. For these reasons, the order of the Assistant Collector and the consequent demands are liable to be quashed". - [1985 (22) ELT 726 (RAJ)].

III. OFFENCES AND PROSECUTION PROVISIONS (SECTION 132 TO 140A)

The Customs Act, 1962 contains the following provisions in regard to offences and prosecutions:-

(A) FALSE DECLARATION, FALSE DOCUMENTS, ETC. [SECTION 132]

Whosoever makes, signs or uses, or causes to be made, signed or used, any declaration, statement or document in the transaction of any business relating to the customs, knowing or having reason to believe that such declaration, statement or document is false in any material particular, shall be punishable with imprisonment for a term which may extend to two years, or with fine, or with both (Section 132).

(B) OBSTRUCTION OF OFFICER OF CUSTOMS [SECTION 133]

If any person intentionally obstructs any officer of customs in the exercise of any powers conferred under Act, such person shall be punishable with imprisonment for a term which may extend to 2 years or with fine, or with both (Section 133).

(C) REFUSAL TO BE X-RAYED [SECTION 134]

If any person

- (a) resists or refuses to allow a radiologist to screen or to take X-ray picture of his body in accordance with an order made by a magistrate under Section 103; or
- (b) resists or refuses to allow suitable action being taken on the advice and under the supervision of a registered medical practitioner for bringing out goods liable to confiscation secreted inside his body, as provided in Section 103;

he shall be punishable with imprisonment for a term which may extend to six months, or with fine, or with both (Section 134).

(D) EVASION OF DUTY OR PROHIBITIONS [SECTION 135]

- (1) without prejudice to any action that may be taken under the Customs Act, if any person –
 - (a) is in relation to any goods in any way knowingly concerned in mis-declaration of value or in any fraudulent evasion or attempt at evasion of any - duty chargeable thereon or of any prohibition for the time being imposed under this Act or any other law for the time being in force with respect to such goods, or
 - (b) acquires possession of or is in any way concerned in carrying, removing, depositing, harbouring, keeping, concealing, selling or purchasing or in any other manner dealing with any goods which he knows or has reason to believe are liable to confiscation under Section 111 or Section 113, as the case may be, or
 - (c) attempts to export any goods which he knows or has reason to believe are liable to confiscation under Section 113.
 - (d) fraudulently availing or attempts to avail of drawback or any exemption from duty provided under this Act in connection with Export of goods

he shall be punishable, -

- (A) Any goods the market price of which exceeds one crore rupees or
- (B) The evasion or attempted evasion of duty exceeding ₹50 lakh rupees
- (C) Such categories of prohibited goods as the Central Government may specify.
- (D) With ₹50 lakh in case of clause (d) referred above.

Provided that in the absence of special and adequate reasons to the contrary to be recorded in the judgment of the Court, such imprisonment shall not be for less than three years;

- (E) in any other case, with imprisonment for a term which may extend to three years or with fine, or with both.
- (2) If any person convicted of an offence under this section or under Sub-section (1) of Section 136 is again convicted of an offence under this section, then he shall be punishable for the second and for every subsequent offence with imprisonment for a term which may extend to seven years and with fine:

In the absence of special and adequate reasons to the contrary to be recorded in the judgement of the court such imprisonment shall not be for less than one year.

- (3) For the purposes of the above provisions the following shall not be considered as special and adequate reasons for awarding a sentence of imprisonment for a term of less than (one year)

namely:-

- (i) the fact that the accused has been convicted for the first time for an offence under this Act;
- (ii) the fact that in any proceeding under this Act, other than a prosecution, the accused has been ordered to pay a penalty or the goods which are the subject matter of such proceedings have been ordered to be confiscated or any other action has been taken against him for the same act which constitutes the offence;
- (iii) the fact that the accused was not the principal offender and was acting merely as a carrier of goods or otherwise was a secondary party to the commission of the offence;
- (iv) the age of the accused.

(E) PREPARATION [SECTION 135A]

If a person makes preparation to export any goods in contravention of the provisions of the Act, and from the circumstances of the case it may be reasonably inferred that if not prevented by circumstances independent of his will, he is determined to carry out his intention to commit the offence, he shall be punishable with imprisonment for a term which may extend to three years, or with fine, or with both (Section 135A).

(F) POWER OF COURT TO PUBLISH NAME, PLACE OF BUSINESS, ETC., OF PERSONS CONVICTED UNDER THE ACT [SECTION 135B]

(1) Where any person is convicted under this Act for contravention of any of the provisions thereof, it shall be competent for the court convicting, the person to cause the name and place of business or residence of such person, nature of the contravention, the fact that the person has been so convicted and such other particulars as the court may consider to be appropriate in the circumstances of the case, to be published at the expense of such person in such newspapers or in such manner as the court may direct.

(2) No publication under Sub-section (1) shall be made until the period for preferring an appeal against the orders of the court has expired without any appeal having been preferred, or such an appeal having been preferred, has been disposed of.

(3) The expenses of any publication under Sub-section (1) shall be recoverable from the convicted person as if it were a fine imposed by the court (Section 135B).

(G) OFFENCES BY OFFICERS OF CUSTOMS [SECTION 136]

(1) If any officer of customs enters into or acquiesces in any agreement to do, abstains from doing, permits, conceals or connives at any act or thing whereby any fraudulent export is effected or any duty of customs leviable on any goods, or any prohibition for the time being in force under this Act or any other law for the time being in force with respect to any goods is or may be evaded, he shall be punishable with imprisonment for a term which may extend to three years or with fine, or with both.

(2) If any officer of customs

- (a) requires any person to be searched for goods liable to confiscation or any document relating thereto, without having reason to believe that he has such goods or documents secreted about this person; or
- (b) arrests any person without having reason to believe that he has been guilty of an offence punishable under Section 135; or
- (c) searches or authorises any other officer of customs to search any place without having reason to

believe that any goods, documents or things of the nature referred to in Section 105 are secreted in that place,

he shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees, or with both.

(3) If any officer of customs, except in the discharge in good faith of his duty as such officer or in compliance with any requisition made under any law for the time being in force, discloses any particulars learnt by him in his official capacity in respect of any goods, he shall be punishable with imprisonment for a term which may extend to six months, or with fine which may extend to one thousand rupees or with both (Section 136).

(H) COGNIZANCE OF OFFENCES [SECTION 137]

(1) No court shall take cognizance of any offence under Section 132, Section 133, Section 134 or Section 135, except with the previous sanction of the Commissioner of Customs.

(2) No court shall take cognizance of any offence under Section 136

- (a) where the offence is alleged to have been committed by an officer of customs not lower in rank than Assistant Commissioner of Customs, except with the previous sanction of the Central Government;
- (b) where the offence is alleged to have been committed by an officer of customs lower in rank than Assistant or Deputy Commissioner of Customs, except with the previous sanction of the Commissioner of Customs (Section 137).

(3) Any offence under this Chapter may, either before or after the institution of prosecution, be compounded by the Chief Commissioner of Customs on payment, by the person accused of offence to the Central Government, of such compounding amount and in such manner of compounding as may be specified by rules.

Provided that nothing contained in this sub-section shall apply to –

- (a) a person who has been allowed to compound once in respect of any offence under Section 135 and 135A;
- (b) a person who has been accused of committing an offence under this Act which is also an offence under any of the following Acts, namely –
 - (i) the Narcotic Drugs and Psychotropic Substances Act, 1985;
 - (ii) the Chemical Weapons Convention Act, 2000;
 - (iii) the Arms Act, 1959;
 - (iv) the Wild Life(Protection) Act, 1972
- (c) a person involved in smuggling of goods certain specified goods
- (d) a person who has been allowed to compound once in respect of any offence under this chapter for goods of value exceeding rupees one crore;
- (e) a person who has been convicted under this Act on or after the 30th day of December, 2005.

(I) OFFENCES TO BE TRIED SUMMARILY [SECTION 138]

Notwithstanding anything contained in the Code of Criminal Procedure, 1973, an offence under this Chapter (other than the offence punishable for a term of imprisonment of three years or more under section 135) may be tried summarily by a Magistrate (Section 138).

(J) PRESUMPTION OF CULPABLE MENTAL STATE [SECTION 138A]

(1) In any prosecution for an offence under this Act which requires a culpable mental state on the part of the accused, the court shall presume the existence of such mental state but it shall be a defence for the accused to prove the fact that he had no such mental state with respect to the act charged as an offence in that prosecution.

Explanation — In this section, “culpable mental state” includes intention, motive, knowledge of a fact and belief in, or reason to believe, a fact.

(2) For the purposes of this section, a fact is said to be proved only when the court believes it to exist beyond reasonable doubt and not merely when its existence is established by a preponderance of probability (Section 138A).

(K) RELEVANCY OF STATEMENTS UNDER CERTAIN CIRCUMSTANCES [SECTION 138B]

(1) A statement made and signed by a person before any gazetted officer of customs during the course of any inquiry or proceeding under this Act shall be relevant, for the purpose of proving, in any prosecution for an offence under this Act, the truth of the facts which it contains, -

- (a) when the person who made the statement is dead or cannot be found, or is incapable of giving evidence, or is kept out of the way by the adverse party, or whose presence cannot be obtained without an amount of delay or expense which, under the circumstances of the case, the court considers unreasonable; or
- (b) when the person who made the statement is examined as a witness in the case before the court and the court is of opinion that, having regard to the circumstances of the case, statement should be admitted in evidence in the interests of justice.

(2) The provisions of Sub-section (1) shall, so far as may be, apply in relation to any proceeding under this Act, other than a proceeding before a court, as they apply in relation to a proceeding before a court (Section 138B).

(L) ADMISSIBILITY OF MICRO FILMS, FASCIMILE COPIES OF DOCUMENTS AND COMPUTERS PRINTOUTS AS DOCUMENTS AND AS EVIDENCE [SECTION 138C]

Section 138C authorises the admissibility of (a) microfilms of documents for the reproduction of image(s) embodied in such microfilms; (b) a facsimile copy of a document; and (c) a computer print-out as admissible evidence in any proceedings under the Customs Law without further requirement of production of the original document itself.

Such acceptance is subject to a series of conditions to safeguard revenue interests, whereby the proper officer is allowed to satisfy himself that such print-outs, facsimiles or micro films do indeed reflect correctly the position as obtained in the original document itself.

(M) PRESUMPTION AS TO DOCUMENTS IN CERTAIN CASES [SECTION 139]

Where any document —

- (i) is produced by any person or has been seized from the custody or control of any person, in either case, under this Act or under any other law, or
- (ii) has been received from any place outside India in the course of investigation of any offence alleged

to have been committed by any person under this Act,

and such document is tendered by the prosecution in evidence against him and any other person who is tried jointly with him, the court shall —

- (a) presume, unless the contrary is proved, that the signature and every other part of such document which purports to be in the handwriting of any particular person or which the court may reasonably assume to have been signed by, or to be in the handwriting of, any particular person, is in that person's handwriting, and in the case of a document executed or attested, that it was executed or attested by the person by whom it purports to have been so executed or attested;
- (b) admit the document in evidence, notwithstanding that it is not duly stamped, if such document is otherwise admissible in evidence;
- (c) in a case falling under clause (i) also presume, unless the contrary is proved, the truth of the contents of such document.

Explanation - For the purposes of this section, "document" includes inventories, photographs and lists certified by a Magistrate under Sub-section(1C) of Section 110 (Section 139).

(N) OFFENCES BY COMPANIES [SECTION 140]

(1) If the person committing an offence under this Chapter is a company, every person who, at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly:

Provided that nothing contained in this sub-section shall render any such person liable to such punishment provided in this Chapter if he proves that the offence was committed without his knowledge or that he exercised all due diligence to prevent the commission of such offence.

(2) Notwithstanding anything contained in Sub-section (1), where an offence under this Chapter has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any negligence on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer should be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Explanation - For the purposes of this section, —

- (a) "company" means a body corporate and includes a firm or other association of individuals; and
- (b) "director", in relation to a firm, means a partner in the firm (Section 140).

(O) APPLICATION OF SECTION 562 OF THE CODE OF CRIMINAL PROCEDURE, 1898, AND OF THE PROBATION OF OFFENDERS ACT, 1958

(1) Nothing contained in Section 562 of the Code of Criminal Procedure, 1898 (5 of 1898), or in the Probation of Offenders Act, 1958 (20 of 1958), shall apply to a person convicted of an offence under the Customs Act unless that person is under eighteen years of age.

(2) The provisions of Sub-section (1) shall have effect notwithstanding anything contained in Sub-section (3) of Section 135 (Section 140A).

SELF TEST QUESTIONS

(These are meant for recapitulation only. Answers to these questions need not to be submitted for evaluation).

1. What are the provisions under Customs Act, regarding the search of suspected persons?
2. What are the powers of Customs Officer with regard to search of premises and stoppage and search of conveyance?
3. What are the provisions with regard to confiscation of improperly imported goods and penalty thereon ?
4. When does an exporter is liable for confiscation of goods and penalty thereon as per the provisions of Customs Act, 1962?
5. When does a conveyance used for import or export of goods is liable for confiscation?
6. What is the liability of the owner of the confiscated conveyance and how he can get relieved of the same ?
7. What are the provisions with regard to confiscation of smuggled goods in case such goods are mixed with other goods or are repacked or are changed in form etc.?
8. What provisions are made under the Customs Act, 1962 to deal with various kinds of offences of Customs?
9. Can a mere preparation towards an act of offence of Customs laws be punished under the Act? State the circumstances.
10. What are the provisions under Customs Act, regarding the power of Court to publish name, place of business, etc. of persons convicted under the Act?
11. When can a Court take cognizance of an offence committed under the Customs Act, 1962?
12. What are the provisions under the Customs Act, with regard to use of Statements, and documents as evidence during prosecution for an offence of Customs?

SUGGESTED READINGS

- (1) Customs Law Manual — *R. K. Jain*
- (2) Indirect Taxes—Law and Practice — *V.S. Datey*

Lesson 7

Advance Ruling, Settlement Commission and Appellate Procedure

LESSON OUTLINE

This Part is divided into three parts:

- ADVANCE RULING
- SETTLEMENT COMMISSION
- APPELLATE PROCEDURE

LEARNING OBJECTIVES

After completion of this lesson the student will have the understanding of

- Provisions of Advance Ruling
- Who can seek advance ruling and on whom it is binding
- What is the procedure to obtain advance ruling
- Procedure to file appeal before the Settlement Commission
- Cases where the application can be made before the Settlement Commission
- Appellate procedures

Important Note: The student may note that these topics are common for Central Excise, Customs and Service Tax. Here, we will discuss the provisions pertaining to Central Excise and Customs only.

ADVANCE RULING

Appreciating the need for foreign investors to be assured in advance of their likely indirect tax liability, the Central Government has set up an Authority for Advance Rulings (Central Excise, Customs and Service Tax) to provide binding ruling on important issues so that intending investors will have a clear-cut indication of their duty liability in advance. The legal provisions relating to advance rulings were introduced in the Finance Act of 1999 and expanded to include Service Tax within its ambit in the Finance Act, 2003.

The advance rulings scheme has the following advantages:

- (a) It ensures clarity and certainty of the tax liability under the Central Excise, Customs and Service Tax laws in advance in relation to an activity (means import or export under the Customs Act, production or manufacture of goods under the Central Excise Act and service to be provided under Finance Act – Service Tax) proposed to be undertaken by the applicant.
- (b) Finality and thereby avoidance of protracted litigation.
- (c) Speedy decisions.
- (d) Inexpensive process.
- (e) Transparency.

The following are the provisions of Central Excise Law and Customs Law pertaining to advance ruling.

	<i>Central Excise Law</i>	<i>Custom Law</i>
Chapter	Chapter 3A	Chapter 5B
Definitions	Section 23A	Section 28E
Authority for advance rulings	Defined under section 23A(e)	Section 28F
Vacancies, etc., not to invalidate proceedings	Section 23B	Section 28G
Application for advance ruling	Section 23C	Section 28H
Procedure on receipt of application	Section 23D	Section 28I
Applicability of advance ruling	Section 23E	Section 28J
Advance ruling to be void in certain circumstances	Section 23F	Section 28K
Powers of Authority	Section 23G	Section 28L
Procedure of Authority	Section 23H	Section 28M

Definitions [Section 23A (Central Excise) & 28E(Custom)]

- (a) **Activity:** As per section 23A(a) “**activity**” means production or manufacture of goods and includes any new business of production or manufacture proposed to be undertaken by the existing producer or manufacturer, as the case may be.

As per section 28E(a) of Customs Act, "activity" means import or export and includes any new business of import or export proposed to be undertaken by the existing importer or exporter, as the case may be.

(b) "**advance ruling**" means the determination, by the authority of a question of law or fact specified in the application regarding the liability to pay duty in relation to an activity proposed to be undertaken, by the applicant;

(c) "**applicant**" means--

- (i) (a) a non-resident setting up a joint venture in India in collaboration with a non-resident or a resident; or
- (b) a resident setting up a joint venture in India in collaboration with a non-resident; or
- (c) a wholly owned subsidiary Indian company, of which the holding company is a foreign company, who or which, as the case may be, proposes to undertake any business activity in India;
- (ii) a joint venture in India; or
- (iii) a resident falling within any such class or category of persons, as the Central Government may, by notification in the Official Gazette, specify in this behalf, and which or who, as the case may be, makes application for advance ruling under sub-section (1) of section 23C or sub-section (1) of 28H;

As per explanation "joint venture in India" means a contractual arrangement whereby two or more persons undertake an economic activity which is subject to joint control and one or more of the participants or partners or equity holders is a non-resident having substantial interest in such arrangement;

(d) "**application**" means an application made to the Authority under sub-section (1) of section 23C or sub-section (1) of 28H;

(e) "**Authority**" means the Authority for Advance Rulings, constituted under sub-section (1), or authorised by the Central Government under sub-section (2A), of section 28F of the Customs Act, 1962 (52 of 1962).

As per section 28E(e), "Authority" means the2[Authority for Advance Rulings (Central Excise, Customs and Service Tax)] constituted under section 28F

(f) "**non-resident**", "Indian company" and "foreign company" shall have the meanings respectively assigned to them in clauses (30), (26) and (23A) of section 2 of the Income-tax Act, 1961(43 of 1961).

AUTHORITY FOR ADVANCE RULINGS (SECTION 28F)

(1) The Central Government shall, by notification in the Official Gazette, constitute an Authority for giving advance rulings, to be called as the Authority for Advance Rulings (Central Excise, Customs and Service Tax).

(2) The Authority shall consist of the following Members appointed by the Central Government, namely:-

- (a) a Chairperson, who is a retired Judge of the Supreme Court;
- (b) an officer of the Indian Customs and Central Excise Service who is qualified to be a Member of the Board;
- (c) an officer of the Indian Legal Service who is, or is qualified to be, an Additional Secretary to the Government of India.

(2A) Notwithstanding anything contained in sub-sections (1) and (2), or any other law for the time being in

force, the Central Government may, by notification in the Official Gazette, authorise an Authority constituted under section 245O of the Income-tax Act, 1961 (43 of 1961), to act as an Authority under this Chapter.

(2B) On and from the date of publication of notification under sub-section (2A), the Authority constituted under sub-section (1) shall not exercise jurisdiction under this Chapter.

(2C) For the purposes of sub-section (2A), the reference to "an officer of the Indian Revenue Service who is qualified to be a Member of Central Board of Direct Taxes" in clause (b) of sub-section (2) of section 245-O of the Income-tax Act, 1961 (43 of 1961) shall be construed as reference to "an officer of the Indian Customs and Central Excise Service who is qualified to be a Member of the Board".

(2D) On and from the date of the authorisation of Authority under sub-section (2A), every application and proceeding pending before the Authority constituted under sub-section (1) shall stand transferred to the Authority so authorised from the stage at which such proceedings stood before the date of such authorisation.

(3) The salaries and allowances payable to, and the terms and conditions of service of, the Members shall be such as the Central Government may by rules determine.

(4) The Central Government shall provide the Authority with such officers and staff as may be necessary for the efficient exercise of the powers of the Authority under this Act.

(5) The office of the Authority shall be located in Delhi.

APPLICATION FOR ADVANCE RULING [SECTION 23C (CENTRAL EXCISE) & 28H(CUSTOM)]

(1) An applicant desirous of obtaining an advance ruling under this Chapter may make an application in such form and in such manner as may be prescribed, stating the question on which the advance ruling is sought.

Questions on which Advance Ruling can be sought

Particulars	Central Excise	Customs
<i>Classification</i>	(a) classification of any goods under the CETA, 1985	(a) classification of goods under the CTA, 1975
<i>Applicability of Exemption Notification</i>	(b) applicability of a notification issued under section 5A(1) having a bearing on the rate of duty;	(b) applicability of a notification issued under section 25(1), having a bearing on the rate of duty;
<i>Valuation of excisable goods/imported or export goods</i>	(c) the principles to be adopted for the purposes of determination of value of the goods	(c) the principles to be adopted for the purposes of determination of value of the goods
<i>Applicability of notification</i>	(d) Notifications issued, in respect of duties of excise under this Act, the CETA, 1985 and any duty chargeable under any other law for the time being in force in the same manner as duty of excise leviable.	(d) Applicability of notifications issued in respect of duties under this Act, the CTA, 1975 and any duty chargeable under any other law for the time being in force in the same manner as duty of customs leviable.
<i>CENVAT Credit</i>	(e) Admissibility of credit of service tax paid or deemed to have been paid on input service or excise duty paid or	

	deemed to have been paid on the goods used in or in relation to the manufacture of the excisable goods.	Not applicable
<i>Payment of duty</i>	(f) Determination of the liability to pay duties of excise on any goods.	Not applicable
<i>Origin of goods</i>	Not applicable	(e) determination of origin of the goods in terms of the rules notified under the CTA, 1975

Fees: The application shall be made in quadruplicate and be accompanied by a fee of two thousand five hundred rupees.

Withdrawal of application: An applicant may withdraw an application within thirty days from the date of the application.

PROCEDURE ON RECEIPT OF APPLICATION [SECTION 23D & SECTION 28I]

On receipt of an application, the Authority shall cause a copy thereof to be forwarded to the Commissioner of Central Excise or Commissioner of Customs and, if necessary, call upon him to furnish the relevant records.

However, where any records have been called for by the Authority in any case, such records shall, as soon as possible, be returned to the Commissioner of Central Excise Commissioner of Customs.

Allow or reject the application:

The Authority may, after examining the application and the records called for, by order, either allow or reject the application:

However, the Authority shall not allow the application where the question raised in the application is,--

- (a) already pending in the applicant's case before any Central Excise Officer or Custom officer, the Appellate Tribunal or any Court;
- (b) the same as in a matter already decided by the Appellate Tribunal or any Court :

However, no application shall be rejected unless an opportunity has been given to the applicant of being heard.

Where the application is rejected, reasons for such rejection shall be given in the order.

A copy of every order shall be sent to the applicant and to the Commissioner of Central Excise or Commissioner of Customs.

Where an application is allowed, the Authority shall, after examining such further material as may be placed before it by the applicant or obtained by the Authority, pronounce its advance ruling on the question specified in the application.

On a request received from the applicant, the Authority shall, before pronouncing its advance ruling, provide an opportunity to the applicant of being heard, either in person or through a duly authorised representative.

"authorised representative" shall have the meaning assigned to it in sub-section (2) of section 35Q.

The Authority shall pronounce its advance ruling in writing within 90 days of the receipt of application.

A copy of the advance ruling pronounced by the Authority, duly signed by the Members and certified in the prescribed manner shall be sent to the applicant and to the Commissioner of Central Excise or Commissioner of Customs, as soon as may be, after such pronouncement.

APPLICABILITY OF ADVANCE RULING (SECTION 23E OR SECTION 28J)

The advance ruling pronounced by the Authority shall be binding only—

- (a) on the applicant who had sought it;
- (b) in respect of any matter referred to in 23C(2) or 28H(2);
- (c) on the Commissioner of Central Excise or Commissioner of Customs, and the Central Excise authorities or the customs authorities subordinate to him, in respect of the applicant.

The advance ruling shall be binding unless there is a change in law or facts on the basis of which the advance ruling has been pronounced.

ADVANCE RULING TO BE VOID IN CERTAIN CIRCUMSTANCES (SECTION 23F OR SECTION 28K)

Where the Authority finds, on a representation made to it by the Commissioner of Central Excise or Commissioner of Customs or otherwise, that an advance ruling pronounced by it has been obtained by the applicant by fraud or misrepresentation of facts, it may, by order, declare such ruling to be *void Ab initio* and thereupon all the provisions of this Act shall apply (after excluding the period beginning with the date of such advance ruling and ending with the date of order under this sub-section) to the applicant as if such advance ruling had never been made.

A copy of the order made shall be sent to the applicant and the Commissioner of Central Excise or Commissioner of Customs.

POWERS OF AUTHORITY (SECTION 23G OR SECTION 28L)

The Authority shall, for the purpose of exercising its powers regarding discovery and inspection, enforcing the attendance of any person and examining him on oath, issuing commissions and compelling production of books of account and other records, have all the powers of a civil court under the Code of Civil Procedure, 1908 (5 of 1908).

The Authority shall be deemed to be a civil court for the purposes of section 195, but not for the purposes of Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974), and every proceeding before the Authority shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purpose of section 196 of the Indian Penal Code (45 of 1860).

PROCEDURE OF AUTHORITY (SECTION 23H OR SECTION 28M)

The Authority shall, subject to the provisions of this Chapter, have power to regulate its own procedure in all matters arising out of the exercise of its powers under this Act.

SETTLEMENT COMMISSION

The disputes under excise and customs are sought to be settled by the commission expeditiously without much strain. The provisions were introduced in the Finance Act, 1998. Under this, cases are settled by the commission at the instance of the assessee who wants to accept liability without contesting the case.

The following are the provisions of Settlement Commission under Central Excise Law and Custom law:

	Central Excise	Custom Law
Chapter	Chapter 5	Chapter 14A
Definition	Section 31	Section 127A
Customs and Central Excise Settlement Commission	Section 32	—
Jurisdiction and powers of Settlement Commission	Section 32A	—
Vice-Chairman to act as Chairman or to discharge his functions in certain circumstances	Section 32B	—
Power of Chairman to transfer cases from one Bench to another	Section 32C	—
Decision to be by majority	Section 32D	—
Application for settlement of cases	Section 32E	Section 127B
Procedure on receipt of application under section 127B	Section 32F	Section 127C
Power of Settlement Commission to order provisional attachment to protect revenue	Section 32G	Section 127D
Power of Settlement Commission to reopen completed proceedings	Section 32H	Section 127E
Power and procedure of Settlement Commission	Section 32I	Section 127F
Inspection etc., of reports	Section 32J	Section 127G
Power of Settlement Commission to grant immunity from prosecution and penalty	Section 32K	Section 127H
Power of Settlement Commission to send a case back to the proper officer	Section 32L	Section 127I
Order of settlement to be conclusive	Section 32M	Section 127J
Recovery of sums due under order of settlement	Section 32N	Section 127K
Bar on subsequent application for settlement in certain cases	Section 32O	Section 127L
Proceedings before Settlement Commission to be judicial proceedings	Section 32P	Section 127M
Certain persons who have filed appeals to the Appellate Tribunal entitled to make applications to the Settlement	Section 32PA	Section 127MA

DEFINITIONS (SECTION 31 & 127A)

"Assessee" means any person who is liable for payment of excise duty assessed under this Act or any other Act and includes any producer or manufacturer of excisable goods or a registered person under the rules made under this Act, of a private warehouse in which excisable goods are stored [Section 31(a)].

"Case" means any proceeding under this Act or any other Act for the levy, assessment and collection of excise duty, pending before an adjudicating authority on the date on which an application under sub-section (1) of section 32E is made:

Provided that when any proceeding is referred back in any appeal or revision, as the case may be, by any court, Appellate Tribunal or any other authority, to the adjudicating authority for a fresh adjudication or decision, as the case may be, then such proceeding shall not be deemed to be a proceeding pending within the meaning of this clause [Section 31(c)]

As per section 127A(b) of Customs Act, 1962, "case" means any proceeding under this Act or any other Act for the levy, assessment and collection of customs duty, or any proceeding by way of appeal or revision in connection with such levy, assessment or collection, which may be pending before a proper officer or the Central Government on the date on which an application under sub-section (1) of section 127B is made :

Provided that where any appeal or application for revision has been preferred after the expiry of the period specified for the filing of such appeal or application for revision under this Act and which has not been admitted, such appeal or revision shall not be deemed to be a proceeding pending within the meaning of this clause;

"Settlement Commission" means the Customs and Central Excise Settlement Commission constituted under section 32; [Section 31(g) and Section 127A(f)]

CONSTITUTION AND COMPOSITION OF SETTLEMENT COMMISSION

The Central Government has constituted the Customs and Central Excise Settlement Commission under Section 32 of the Central Excise Act. The commission has principal Bench at Delhi and additional Benches at other three major metros. The principal Bench is headed by the chairman and the others by the vice-chairman. Two other members will be assisting them at each bench.

The commission provides quick and easy settlement of tax disputes involving high revenue stake. The purpose is to save time and energy of both the tax payer and the Department. The procedure followed by the commission is much less costly and is beneficial to the assessee.

POWERS OF THE COMMISSION

The commission will exercise its powers for settling the cases as a bench consisting of three members, and all decisions will be by majority. The Chairman has the power to constitute a large bench or special bench, wherever necessary. The commission has power to regulate its own procedures and procedures of its benches.

The commission has power to have exclusive jurisdiction to exercise the powers and perform the functions of any officer of customs/excise.

The commission can grant immunity from prosecution for any offence under Central Excise Act/Customs Act. It can also withdraw the immunity granted if the conditions specified under its order are not complied with.

The commission has power to grant waiver either wholly or in part from imposition of any penalty, fine, but NOT interest under excise/customs in respect of the case covered under the settlement.

It can order provisional attachment of property belonging to the applicant if found necessary to protect the interests of the revenue.

Note: The order of the Commission is conclusive and cannot be re-opened in any proceedings under the Acts.

APPLICATION TO THE COMMISSION [SECTION 127B]

The following categories of people fulfilling the requirements can make an application for settlement

commission:

- An importer/exporter or a manufacturer can approach the settlement commission by filing an application in the prescribed form. It may be noted that the department cannot approach the commission for settlement.
- The application can only be made to admit the liability, not to contest it. The admitted liability shall be more than ₹ 3,00,000.
- The applicant can file an application in the following cases:
 - Admission of short levy on account of misclassification.
 - Under valuation.
 - Inapplicability of exemption notification/CENVAT credit.

Note:

Application can not be made in case where no return has been filed.

The applicant has to deposit the additional duty with interest along with the application.

An application has only one opportunity to avail the settlement in his lifetime.

The exporter under DEEC, EOU/EPZ can approach the commission if he failed to fulfill his export obligation for reasons beyond his control.

Even an SSI units can approach the commission.

The cases involving the valuation dispute can be taken up with the commission.

Cases relating to interpretation of law and notifications can be taken up.

Persons involved in the following cases cannot approach the commission for settlement:

- Cases involving narcotic drugs and psychotropic substances under Narcotic Drugs and Psychotropic Substances Act, 1985.
- Cases where the revenue has invoked the provisions of Section 123 of the Customs Act (seizure of smuggled goods and burden of proof).
- Cases involving interpretation of classification of goods under the Customs Tariff Act or CETA.
- Cases pending before the Tribunal/Court.
- Cases remanded by the tribunal for fresh adjudication.

PROCEDURE ON RECEIPT OF AN APPLICATION UNDER SECTION 127B [SECTION 127C]

- The application is to be submitted to the commission in the prescribed form with the fee and the commission will issue a dated acknowledgement immediately.
- A report is called for from the department which the department is supposed to submit within one month of receiving the communication.
- Intimation of hearing shall be issued within 2 months of receiving application.
- The proceedings will be in camera (personal, not in public).
- Only after admitting the case, the commission will open the sealed cover submitted by the applicant containing the incriminating information.

- Thereafter, the sealed cover is sent to the verification of the department. On receiving the report from the department it will proceed to decide the matter and the applicant has to deposit the amount within 30 days of order of the commission.

APPELLATE PROCEDURES

Decisions made or orders passed by Officers of Central Excise at different levels can give rise to grievances which broadly are of two kinds. First, if the decision denies to the assessee the benefit due, or confers a hardship undue, it can create a grievance to him. Secondly, the decisions can confer on the assessee a benefit undue or deny revenues due to the Government, in which case the Government itself becomes the aggrieved party. There are two parties to every dispute, and it happens at times that satisfaction to one could mean dissatisfaction to the other. There should be mechanism to go into grievances of either kind and the appellate mechanism is meant precisely for that.

The judiciary is no doubt the agency before which relief can be sought by the citizen in matters of implementation or enforcement of any law, including laws pertaining to Central Excise and Customs. However, fiscal statutes like the Central Excise Act, 1944 and the Customs Act, 1962 contain provisions and constitute organisations within the departments themselves to enable settlement of such disputes, if possible, without the need to seek judicial remedy. The need for fiscal enactments to provide "in house" facilities, so to say, to seek redressal of grievances arises due to the fact that by the very nature of such laws, and the dimensions of the field that they cover, the number of disputes which emerge is so huge as to make it a very difficult proposition for the judiciary alone to deal with. Further, the judicial process is expensive and time consuming and hence unviable if the judiciary alone is made the resort to citizens. Statutory provisions pertaining to appeals are contained in Chapter VI-A of the Central Excise Act, 1944 (Sections 35 and 36) inserted by the Finance Act, 1980 and came into force on 11.10.1982.

Following are the common provisions pertaining to Central Excise Law and Customs Law:

APPEALS	Chapter 6A	Chapter 15
- Appeals to Commissioner Appeals	Section 35	Section 128
- Procedure in appeal	Section 35A	Section 128A
- Appellate Tribunal	---	Section 129
- Appeals to the Appellate Tribunal	Section 35B	Section 129A
- Orders of Appellate Tribunal	Section 35C	Section 129B
- Procedure of Appellate Tribunal	Section 35D	Section 129C
- Power of Board Commissioner of Customs to pass certain orders	Section 35E	Section 129D
- Powers of revision of Board or Commissioner of Customs in certain cases	Section 35EA	Section 129DA
- Revision by Central Government	Section 35EE	Section 129DD
- Deposit, pending appeal, of duty and interest demanded or penalty levied	Section 35F	Section 129E

- Interest on delayed refund of amount deposit under the Proviso to Section 129E or section 35F	Section 35FF	Section 129 EE
- Statement of case to High Court	Section 35G	Section 130
- Statement of case to Supreme Court in certain cases	Section 35H	---
- Application to High Court	---	Section 130A
- Power of High Court or Supreme Court to require statement to be amended	Section 35-I	Section 130B
- Case before High Court to be heard by not less than two judges	Section 35J	Section 130C
- Decision of High Court or Supreme Court on the case stated	Section 35K	Section 130D
- Appeal to Supreme Court	Section 35L	Section 130E
- Hearing before Supreme Court	Section 35M	Section 130F
- Sums due to be paid notwithstanding reference, etc	Section 35N	Section 131
- Exclusion of time taken for copy	Section 35-O	Section 131A
- Transfer of certain pending proceedings and transitional provisions	Section 35P	Section 131B
- Appearance by authorised representative	Section 35Q	---
- Appeal not to be filed in certain cases	Section 35R	Section 131BA
- Definitions	Section 36	Section 131C [Omitted]

APPELLATE SCHEME UNDER CENTRAL EXCISE

The appellate scheme in Central Excise comprises three institutions viz. Commissioner (Appeals); the Customs, Excise and Service Tax Appellate Tribunal (CESTAT); and the Government of India as revisionary authority. The principle inbuilt into the scheme is that for an appeal to lie before a particular authority, it should have been passed by authorities lower in rank within the department to the appellate authority. The table below, bringing out the stages of appeal in regard to orders passed by each authority will indicate how this principle is incorporated in the appellate scheme.

	Orders passed by	Relief at first stage	Relief at second stage
(a)	Superintendent/Assistant Deputy/Additional/Joint Commissioner	Appeal before Commissioner (Appeals)	Appeal before CESTAT
(b)	Commissioner	Appeal before CESTAT	Appeal before CESTAT

MONETARY LIMITS FOR FILING OF APPEAL

With effect from 1.9.2011, the CBEC has issued instruction regarding the monetary limits below which

appeal should not be filed by the department in the Tribunal, High Courts and the Supreme Court as under:

Sl. No.	Appellate Forum	Monetary Limit (₹)
1.	CESTAT	5,00,000
2.	High Courts	10,00,000
3.	Supreme Court	25,00,000

The Board has clarified that for ascertaining whether a matter would be covered within or without the aforementioned limits, the determinative element would be duty/tax under dispute, e.g., in a case involving duty of ₹5,00,000 or below with equal penalty and interest, as the case may be, no appeal can be filed in the Tribunal. Similarly no appeal would be filed in the High Court if the duty involved does not exceed ₹10 lakhs with or without penalty and interest. The monetary limit would apply to cases of refund as well.

APPEALS BEFORE COMMISSIONER (APPEALS) [SECTION 35]

Under Section 35(1) any person aggrieved by any decision or order passed under the Act by an officer lower in rank than a Commissioner may file appeal to the Commissioner (Appeals). The time limit for filing an appeal is sixty days from the date of communication of the order contested. This period of sixty days may further be extended by the Commissioner appeal for 30 days on showing the sufficient cause.

The word "communication" used in this section would mean actual receipt by the appellant, of the order impugned. The Commissioner may adjourn an appeal or grant time to parties as the case may be. However, no such adjournment shall be granted more than three times to a party during hearing of the appeal.

PROCEDURE FOR FILING APPEAL BEFORE COMMISSIONER (APPEALS)

The appeal should be filed in Form EA-I in duplicate and should be accompanied by a copy of the order or decision appealed against. While the statutorily prescribed form should invariably be filed, if the appellant desires to make his grounds more elaborate, there is no bar to his doing so by attaching extra sheets. In his own interest, the appellant must make his case in a clear, comprehensive and self-contained manner, adducing all the arguments and submitting all the evidence along with the appeal. However, if compulsions of time limit for filing the appeal render this difficult, he may make a suitable indication in the appeal that further elaboration/evidence will be sent separately. If the constraints of the columns in the prescribed form render it difficult to explain the grounds, an indication can be made in the form to the effect that the grounds of appeal are enclosed, and the grounds can be elaborated in separate sheets annexed to the proforma. The requirement is only that without the proforma duly completed, the appeal will not be accepted.

While filing the appeal which can be either by tendering it in the Office of the Commissioner (Appeals) or by sending it by Registered Post Acknowledgement Due, the appellant must make sure that in either case, he gets possession of a dated acknowledgement of receipt. This is of crucial importance since if the appeal is time barred, it will be rejected on that ground alone, without the merits being looked into.

Apart from making the grounds in writing, the appellant can also seek the facility of being heard in person by the Commissioner (Appeals) before the appeal is decided upon. Section 35-A(1) makes it mandatory that personal hearing should be granted whenever asked for. For the hearing, the appellant may either appear in person or through a counsel authorised for such purposes.

The appeal filed will be examined in the Office of the Commissioner (Appeals) on the basis of the records pertaining to the decision impugned. If a personal hearing has been asked for, the Commissioners (Appeals) will decide the date and time, and an intimation sufficiently in advance will be sent to the appellant/counsel. Failure to present oneself for personal hearing on the date and time fixed may result in the appeal being

decided on the basis of the written plaint alone.

However, if there are any insurmountable difficulties in appearing on the date, intimation should be given to the Commissioner (Appeals) before the date fixed for hearing, and a revised date/time is requested for and obtained.

Even if a counsel is engaged, there is no bar to the appellant also presenting himself and explaining his case. A record of the submissions made during the hearing will be made, and this will form an integral part of the appellate order eventually issued. The practice followed by most Commissioners (Appeal) is to make a record of the hearing and obtain the signature of the party heard thereon before proceeding to decide the appeal. This should give satisfaction to the appellant that the record reflects all the submissions made, in a correct manner. If the appellant feels that the record does not correctly reflect all the arguments made during the hearing, he would be well advised to bring this immediately to the notice of the Commissioner (Appeals) for rectification of the record.

While normally, a personal hearing is meant for elaboration of the grounds already made in the written plaint, Section 35A(2) authorises the Commissioner (Appeals) at the time of hearing of the appeal, to allow the appellant even to go into grounds not specified earlier in the written appeal, provided the Commissioner (Appeals) is satisfied that the omission of the ground earlier was not wilful or unreasonable.

After the hearing is completed, the Commissioner (Appeals) will decide the case on the basis of all the facts and evidence on record and issue the order in appeal. It should be a “speaking order” in the sense that not only the decision but also the detailed reasoning for the decision should be incorporated therein and communicated to the appellant. Section 35A(4) makes this a statutory requirement.

The order issued by the Commissioner (Appeals) may confirm, modify or annul the order appealed against (the original order) as provided in Section 35A(3) after such inquiry as he may think just and proper. While any appellate order confirming, modifying or annuling the original order implies that the appeal is decided on merits, the Commissioner (Appeals) may also refrain from doing these.

While appeals are normally filed seeking relief, there is no bar to the Commissioner (Appeals) not only giving relief, but even causing further privations to the party. The two provisos to Section 35A(3) authorise this. The Commissioner (Appeals) can enhance any penalty or fine or confiscate goods of value greater than what had been confiscated by the original authority, or reduce the amount of refund. However, if he contemplates taking any such action, it can only be after putting the appellant on notice, and giving him reasonable opportunity to oppose the proposed decision. Similarly, the Commissioner (Appeals) if he is of the opinion that certain duties are due to the department but had not accrued can order payment of such sums, provided a notice is issued for demanding the duty within the time limit prescribed under Section 11A.

As provided in Section 35A(4A), the Commissioner (Appeals) may, where it is possible to do so hear and decide every appeal within a period of six months from the date on which it is filed.

CUSTOMS, EXCISE AND SERVICE TAX APPELLATE TRIBUNAL

To ensure safeguards to citizens' interests in any area of administration, including fiscal administration, it is essential that appellate authorities are totally independent of the administrative authorities. Till a few years back, the appellate mechanism in Central Excise was liable to critical comment in this regard, since the appellate remedies then provided in the statute culminated in the Central Board of Excise and Customs itself acting as an appellate agency. The Board, in this manner, combined the functions of the administrative as well as the appellate authority in the department. Though the Board, manned by very senior officers in the department, maintained the highest standards of objectivity in considering appeals, was still prone to give rise to widespread misgivings in the minds of trade and industry regarding the possibility of a 'revenue bias' in its approach as an appellate body. A number of Committees and Commissions set up by the Government

from time to time, such as the Central Excise Reorganization Committee, the Tariff Revision Committee, etc. took stock of the position and suggested the setting up of an independent Tribunal on the lines already available in regard to Income Tax, so that such misgivings may be dispelled, and confidence created in the minds of the assessees as a whole.

The department eventually decided to set up the Tribunal and the necessary legislation was made in 1980 [Section 50 of the Finance (No. 2) Act, 1980]. The legislation was implemented from 11.10.1982, the date of implementation being announced through Notification No. 214/82-CE dated 10.9.1982.

The Tribunal can also deal with the cases under service tax. However, it is not vested with the powers of review.

(1) COMPOSITION OF THE TRIBUNAL

As with the Income Tax Appellate Tribunal, CESTAT comprises technical members and judicial members, the underlying idea being that the former would provide the forum, the benefit of their knowledge and experience in the Department, and the latter will contribute benefits arising from unalloyed judicial approach. At present, the CESTAT functions in Delhi, Kolkata, Chennai, Mumbai and Bangalore.

The CESTAT is presided over by a President, with one or more Vice Presidents. As for members, the technical members are very senior officers of the rank of Commissioners of Central Excise and Customs, whereas the judicial members are senior members of the bench or the bar, selected for appointment.

As indicated in the statement at the very beginning, appellate orders decided by Commissioners (Appeals) can be contested before the CESTAT and in such situations, it functions as a second appellate forum. Original orders passed by Commissioner (including Additional Commissioner) can be contested straightaway before the CESTAT. In such situations, it will function as the first and the only appellate forum within the department. Appeals are normally decided on the basis of majority decision. In case a major decision does not arise, the President can nominate an extra member to the bench, to enable a majority decision arising.

To ensure that the valuable time of a body of this nature is not wasted in examining disputes involving insignificant stakes, it has been provided that the CESTAT may, in its discretion, refuse to admit the appeal in respect of any order if the amount of fine or penalty under contest does not exceed ` 50,000/- (Rupees Fifty Thousand only) [Section 35B(1)]. However, if the issue involved pertains to determination of the rate of duty or valuation, the CESTAT cannot refuse to admit the appeal, whatever be the amount involved. Again, to ensure optimum utilisation of the Tribunal's valuable time, Section 35D(3) provides that if the case involves amounts upto ₹ 50,00,000/- (Rupees Fifty Lakh only) in duty/fine/penalty, a single Member (instead of a bench) can himself decide the case.

But where the amount involved is more than ` 10 crore on day to day basis, three member Benches shall be constituted for hearing such cases. All cases involving an amount of ` 25 crores or more would be listed before the Benches on priority basis and would be heard on day to day basis.

(2) FILING APPEAL BEFORE CESTAT (SECTION 35B)

(1) Any person aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order

- (a) A decision or order passed by the [Commissioner] of Central Excise as an adjudicating authority;
- (b) An order passed by the [Commissioner] (Appeals) under Section 35A;
- (c) An order passed by the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 (54 of 1963) (hereafter in this Chapter referred to as the Board) or the Appellate [Commissioner] of Central Excise under Section 35, as it stood immediately before the

appointed day;

- (d) An order passed by the Board or the [Commissioner] of Central Excise, either before or after the appointed day, under Section 35A, as it stood immediately before that day.

Provided that no appeal shall lie to the Appellate Tribunal in respect of any order referred to in clause (b) if such order relates to loss of goods in transit, rebate of duty of excise on goods exported, goods exported outside India (except to Nepal or Bhutan) without payment of duty, credit of any duty allowed to be utilised towards payment of excise duty on final products under the provisions of this Act or the rules made there under and such order is passed by the Commissioner (Appeals) on or after the date appointed.

Provided further that the Appellate Tribunal may, in its discretion, refuse to admit an appeal in respect of an order referred to in clause (b) or clause (c) or clause (d) where, the amount of fine or penalty determined by such order does not exceed fifty thousand rupees.

(2) The Committee of Commissioners of Central Excise may, if it is of opinion that an order passed by the Appellate [Commissioner of Central Excise under section 35, as it stood immediately before the appointed day, or the [Commissioner (Appeals) under section 35A], is not legal or proper, direct any Central Excise Officer authorised by him in this behalf to make an appeal to the Appellate Tribunal against such order.

Provided that where the Committee of Commissioners of Central Excise differs in its opinion regarding the appeal against the order of the Commissioner (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Chief Commissioner of Central Excise who shall, after considering the facts of the order, if is of the opinion that the order passed by the Commissioner (Appeals) is not legal or proper, direct any Central Excise Officer to appeal to the Appellate Tribunal against such order.

Explanation: For the purposes of this sub-section, "jurisdictional Chief Commissioner" means the Chief Commissioner of Central Excise having jurisdiction over the adjudicating authority in the matter.

(3) Every appeal under this section shall be filed within three months from the date on which the order sought to be appealed against is communicated to the Commissioner of Central Excise, or, as the case may be, the other party preferring the appeal.

(4) The party against whom the appeal has been preferred may file a memorandum of cross-objections within forty-five days of the receipt of the notice.

(5) The Appellate Tribunal can condone the delay in filing an appeal or memorandum of cross-objections if it is satisfied that there was sufficient cause for not presenting it within that period.

Fees:

An appeal to the Appellate Tribunal shall be in the prescribed form and shall be accompanied by a fee of:

- (a) *Rupees one thousand where the amount of duty and interest demanded and penalty rupees five lakh or less.*
- (b) *Rupees five thousand, where the amount of duty and interest demanded and penalty levied is more than rupees five lakh but not exceeding fifty lakh rupees.*
- (c) *ten thousand rupees, where the amount of duty and interest demanded and penalty levied is more than fifty lakh rupees,*

Provided that no fee shall be payable in the case where an appeal filed by the department or for submitting a memorandum of cross-objections.

(3) APPEARANCE BY AUTHORISED REPRESENTATIVE [SECTION 35Q]:

Both the parties to the dispute will be heard together by the bench. The Department will be represented normally by departmental officers functioning as Departmental Representatives. The assessee can appear in person or through counsel. In this regard, Section 35Q prescribes that any party to a dispute may otherwise than when required by the Tribunal to attend personally for examination on oath, can appear through an authorised representative who may be:

- (a) his relative or regular employee; or
- (b) Custom House Agent; or
- (c) any legal practitioner who is entitled to practice in any civil court; or
- (d) any person who has acquired such qualifications as the Central Government may prescribe by rules made in this behalf. The Central Government has since prescribed the qualifications under Rule 12 of the Central Excise (Appeals) Rules, 2001.

For the purposes of clause (c) of Sub-section (2) of Section 35Q, an authorised representative shall include a person who has acquired any of the following qualifications being the qualifications specified under clause (c) to Rule 12 of the Central Excise (Appeals) Rules, 2001, namely:

- (a) a Chartered Accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949); or
- (b) a Cost Accountant within the meaning of the Cost and Works Accountants Act, 1959 (23 of 1959); or
- (c) a Company Secretary within the meaning of the Company Secretaries Act, 1980 (56 of 1980) who has obtained a certificate of practice under Section 6 of that Act; or
- (d) a post-graduate or an Honours degree holder in Commerce or a post-graduate degree or diploma holder in Business Administration from any recognised university; or
- (e) a person formerly employed in the Department of Customs and Central Excise or Narcotics and has retired or resigned from such employment after having rendered service in any capacity in one or more of the said departments for not less than ten years in the aggregate,

can act as an authorised representative.

(4) DECISIONS BY CESTAT [SECTION 35C]:

The orders passed by the Tribunal may confirm, modify or annul the order appealed against. The Tribunal may also refer the case back to the authority below which passed the order impugned, with such directions as it may deem fit, for fresh decision, taking additional evidence, if necessary. The Tribunal may also at any time within six months from the date of its own order, with a view to rectifying any mistake apparent from the record, amend any order passed by it, and can make such amendments as if the mistake is brought to its notice by Commissioner of Central Excise or the other party to the appeal.

Any amendment made in this manner under Section 35-C(2) enhancing the assessment or reducing the penalty can be made only after giving due notice to the other party.

The appeals shall be heard and decided by the Tribunal within three years from the date of filing of appeal. However, in case where stay order has been made in any proceeding relating to an appeal filed under Section 35B(1), the Tribunal shall dispose of the appeal within one hundred and eighty days from the date of such order. If the appeal is not disposed of within the above period, then on the expiry of the period, the stay order shall stand vacated [Section 35C(2A)].

CESTAT however, has the power to extend the stay beyond 180 days in deserving cases where delay was not attributable to the assessee, the same view was upheld by Supreme Court in CCE v. Kumar Cotton Mills 2005 (180) ELT SC.

The Honourable Supreme Court observed in the above case that the assessee cannot be punished for matters which may be completely beyond control.

No appeal can be filed against the order of the CESTAT granting or refusing stay because it is only an interim order.

However, if the Commissioner (Appeals) dismisses the appeal for non-payment of pre-deposit of duty pending appeal, it is a final order and appeal is allowed against such order before the CESTAT.

(5) STAY PETITIONS BEFORE CESTAT

While as with the Commissioner (Appeals), amounts to be paid as a consequence of the order disputed should be deposited even if an appeal is filed before CESTAT, the aggrieved party can however request the CESTAT for a stay of such deposits. The application for stay should be presented separately in triplicate by the appellant or his Counsel before the Registrar. Naturally, it should substantiate the request for stay with grounds, evidence etc. The applicant himself should serve one copy of the stay petition to the Senior Departmental officer representing the Department before CESTAT. This application for stay will be heard separately by the bench before the appeal is taken up for consideration. The other party (Department) can oppose the request, setting out the case why the requirement of deposit of duty/penalty etc. should not be stayed. The decision made by the bench to grant or refuse the stay is final.

After the appeal is decided, the Registrar will communicate the decision to the Appellant and the other party. The case records will be sent to the Excise Commissionerate to enable immediate implementation of the decision. In this regard, in cases where relief is given to the appellant by the CESTAT certain benches are known at times, to have fixed deadlines for implementation of decision giving relief. If such deadlines are breached by the department, the grievances in such matters can be agitated by the appellant before the concerned bench of the Tribunal.

FURTHER REMEDIES AFTER DECISION BY CESTAT

Orders of the Tribunal on points of facts are final. In all other matters, further remedies as below are available to the aggrieved parties.

1. REFERENCE ON ORDER OF CESTAT

All orders made by CESTAT except those relating to classification and valuation will be appealable before the Honourable High Court if there is a substantial question of law under Section 35G.

Cases relating to classification and valuation shall be taken up directly to the Supreme Court.

The jurisdiction of the High Court to hear appeals continues till the National Tax Tribunal comes into operation.

The appeal shall be made before the Honourable High Court within 180 days of order of CESTAT.

The appeal will be heard by at least by a Division Bench of High Court. In case of difference of opinion by a division bench, it will be referred to the third judge and the majority of the opinion shall prevail.

2. APPEALS AND CONSTITUTIONAL REMEDIES

Appeal to Supreme Court can be made in the following cases:

- (a) any judgement of the High Court delivered—
 - (i) in an appeal made under Section 35G; or
 - (ii) on a reference made under Section 35G by the Appellate Tribunal before the 1st day of July, 2003;
 - (iii) on a reference made under Section 35H, in any case which, on its own motion or on an oral application made by or on behalf of the party aggrieved, immediately after passing of the judgement, the High Court certifies to be a fit one for appeal to the Supreme Court; or
- (b) on an order passed by CESTAT relating to rate of duty/valuation of goods;
- (c) by special leave petition under Article 136 of the Constitution.

Normally, the Supreme Court will entertain appeal only if—

- (a) *a substantial question of law is involved;*
- (b) *a question of general importance is involved;*
- (c) *when manifest injustice is done;*
- (d) *there are conflicting observations of the Supreme Court on same issue;*
- (e) *no authoritative ruling of Supreme Court in the issue.*

Appeal will not be entertained if the Tribunal has acted bona fide with a speaking order and has considered all relevant factors even if another view may be possible.

Our Constitution has maintained a balance between powers of Legislature, Judiciary and Executive. All actions of Government are subject to judicial scrutiny of Supreme Court and High Court, irrespective of any particular statute. These judicial powers are conferred by the Constitution itself and hence cannot be curtailed by any legislation. Declaration in any statute that the order is final does not affect Writ jurisdiction. Powers to issue high prerogative writs are extraordinary discretionary powers and hence are to be exercised sparingly and in a fit case, on sound principles of law. Court will invoke writ jurisdiction only in exceptional cases. Thus, when alternative remedy like departmental appeal or ordinary civil suit is available, writ jurisdiction will not be normally invoked.

POWERS OF COMMITTEE OF CHIEF COMMISSIONERS OF CENTRAL EXCISE OR COMMISSIONER OF CENTRAL EXCISE TO PASS CERTAIN ORDERS ON ITS OWN (SECTION 35E)

(1) The Committee of Chief Commissioners of Central Excise may, of its own motion, call for and examine the record of any proceeding in which a Commissioner of Central Excise as an adjudicating authority has passed any decision or order under this Act for the purpose of satisfying itself as to the legality or propriety of any such decision or order and may, by order, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order as may be specified by the Committee in its order:

Provided that where the Committee of Chief Commissioners of Central Excise differs in its opinion as to the legality or propriety of the decision or order of the Commissioner of Central Excise, it shall state the point or points on which it differs and make a reference to the Board. After considering the facts of the decision or order, if the Board considers that the decision or order passed by the Commissioner of Central Excise is not legal or proper, and then it may, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points.

(2) Similarly, the Commissioner of Central Excise may, of his own motion, call for and examine any proceeding in which the order been issued by adjudicating authority subordinate to him and direct such authority or any Central Excise Officer subordinate to him to make an appeal to the Commissioner (Appeals) for the determination of such points arising out of the decision or order.

(3) Time limit: The Committee of Chief Commissioners of Central Excise or the Commissioner of Central Excise, as the case may be, shall make order under sub-section (1) or sub-section (2) within a period of three months from the date of communication of the decision or order of the adjudicating authority.

DEPOSIT, PENDING APPEAL, OF DUTY DEMANDED OR PENALTY LEVIED (SECTION 35F)

Where in any appeal, the decision or order appealed against relates to any duty demanded in respect of goods which are not under the control of Central Excise authorities or any penalty levied under this Act, the person desirous of appealing against such decision or order shall, pending the appeal, deposit with the adjudicating authority the duty demanded or the penalty levied:

Provided that where in any particular case, the Commissioner (Appeals) or the Appellate Tribunal is of opinion that the deposit of duty demanded or penalty levied would cause undue hardship to such person, the Commissioner (Appeals) or, as the case may be, the Appellate Tribunal, may dispense with such deposit subject to such conditions as he or it may deem fit to impose so as to safeguard the interests of revenue.

Provided further that where an application is filed before the Commissioner (Appeals) for dispensing with the deposit of duty demanded or penalty levied under the first proviso, the Commissioner (Appeals) shall, where it is possible to do so, decide such application within thirty days from the date of its filing.

Explanation: For the purposes of this section “duty demanded” shall include;

- (i) Amount determined under section 11D;
- (ii) Amount of erroneous Cenvat credit taken;
- (iii) Amount payable under rule 57CC of Central Excise Rules, 1944;
- (iv) Amount payable under rule 6 of Cenvat Credit Rules, 2001 or Cenvat Credit Rules, 2002 or Cenvat Credit Rules, 2004;
- (v) Interest payable under the provisions of this Act or the rules made there under.

INTEREST ON DELAYED REFUND OF AMOUNT DEPOSITED UNDER THE PROVISO TO SECTION 35F (SECTION 35FF)

Where an amount deposited by the appellant under the first proviso to section 35F, is required to be refunded consequent upon the order of the appellate authority and such amount is not refunded within three months from the date of communication of such order to the adjudicating authority, unless the operation of the order of the appellate authority is stayed by a superior court or tribunal, there shall be paid to the appellant interest at the rate specified in section 11BB after the expiry of three months from the date of communication of the order of the appellate authority, till the date of refund of such amount.

REVISIONARY ROLE OF THE CENTRAL GOVERNMENT [SECTION 35EE]

Before the Tribunal was set up, the Central Government in the Ministry of Finance (Department of Revenue)

exercised revisionary functions in regard to all cases decided at appeal level within the Department, including the Board. Even after the Tribunal was set up, the revisionary role continues, but within a drastically reduced area of operation. In Central Excise, if the Appellate orders are passed by Commissioner (Appeals) in cases of (a) loss of goods, (b) rebate of duty of excise on goods exported; or (c) export under bond without payment of duty, a Revision Application can be filed before the Central Government (Section 35-EE). However, the Central Government has the discretion to refuse such application where the amount of duty, fine or penalty determined does not exceed five thousand rupees. As would be observed, the original orders in those cases would have been passed by officers below the rank of Commissioner, since only in such case, appeals will be decided by Commissioner (Appeals). Where the Commissioner of Central Excise is of the opinion that an order passed by Commissioner (Appeals) under Section 35A is not legal or proper, he may direct the proper officer to make an application on his behalf to the Central Government for revision of such an order [Section 35EE(1A)]. If the Commissioner himself is the original authority there is no role for the Central Government as a revisionary authority.

In cases as noted above, the Revision Application against the appellate order must be filed within three months from the date of receipt of the appellate order. The period is extendable by the Central Government (on sufficient cause being shown) by a further three months. A fee of ` 200/- (Rupees Two Hundred) where the amount of duty and interest demanded, fine or penalty levied by any Central Excise Officer is rupees one lakh or less and one thousand rupees in case it exceeds one lakh rupees is payable in regard to every Revision Application, and payment should be by crossed cheque to accompany the Revision Application. The applicant should also send a copy of the appellate order contested. The prescribed form for filing the Revision Application is E.A -8. However, no fee is payable where an application is made to the Central Government for revision of an order passed by the Commissioner (Appeals) under Sub-section (1A) of Section 35EE.

On receipt of the Revision Application, it will be examined in the Ministry of Finance, after obtaining the relevant departmental records. Personal hearing, if asked for, will be granted. Decision will be taken at the level of Joint Secretary to the Government of India. As revisionary authority the Central Government also has powers to increase the penalty or demand duty or increase confiscation. However, no such action can be taken without putting the party to notice, and giving him due opportunity for defense. In case the notice is for demanding duty, the time limit of Section 11A (one year/5 years) will apply.

ADJUDICATION AND APPELLATE PROVISIONS UNDER CUSTOM LAWS

Orders passed by adjudicating authorities give rise to disputes between the assessee and Customs Department. These generally arise in connection with the classification and valuation of goods or in regard to infraction of legal provisions and/or procedures. In any tax system, disputes are bound to arise howsoever simple a tariff is made to appear. Burkets famous dictum that it is difficult to tax and please, is known to all.

An incorrect assessment to a duty might take place on account of various factors. It may arise due to inadvertence, error, collusion, or misconstruction on the part of an officer of revenue, or through mis-statement as to the quantity, description or value in respect of dutiable goods on the part of an assessee. An incorrect assessment is as detrimental to the exchequer as it is to the assessee. There are various factors leading to a mistake which result in an incorrect assessment. The Public Accounts Committee [(5th Lok Sabha) (1972-73) 89th Report at P. 14] identified them as mainly resulting from.

The procedure prescribed for filing appeals and revision applications against orders passed by Customs officers are described in Sections 128, 130 and 131 of the Customs Act.

The relevant provisions regarding Appeal and Revision are discussed below, Section-wise.

(A) APPEALS TO COMMISSIONER (APPEALS)(SECTION 128)

- (1) Any person aggrieved by any decision or order passed under this Act by an officer of customs lower in rank than a Commissioner of Customs may appeal to the Commissioner (Appeals) within 60 days from the date of communication to him of such decision or order:

Provided that the Commissioner (Appeals) may, if he is satisfied that the appellant was prevented by sufficient cause from presenting the appeal within the aforesaid period of 60 days, allow it to be presented within a further period of thirty days.

- (2) Every appeal under this section shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf.

PROCEDURE IN APPEAL (SECTION 128A)

- (1) The Commissioner (Appeals) shall give an opportunity to the appellant to be heard if he so desires.
- (2) The Commissioner (Appeals) may, at the hearing of an appeal, allow the appellant to go into any ground of appeal not specified in the grounds of appeal, if the Commissioner (Appeal), is satisfied that the omission of that ground from the grounds of appeal was not willful or unreasonable.
- (3) The Commissioner (Appeals) shall, after making such further inquiry as may be necessary, pass such order as he thinks just and proper, confirming, modifying or annulling the decision or order appealed against.

Provided that an order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value or reducing the amount of refund shall not be passed unless the appellant has been given a reasonable opportunity of showing cause against the proposed order;

Provided further that where the Commissioner (Appeals) is of opinion that any duty has not been levied or has been short-levied or erroneously refunded, no order requiring the appellant to pay any duty not levied, short-levied and erroneously refunded shall be passed unless the appellant is given notice within the time-limit specified in Section 28 to show cause against the proposed order.

- (4) The order of the Commissioner (Appeals) disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision.
- (4A) The Commissioner (Appeals) shall, where it is possible to do so, hear and decide every appeal within a period of six months from the date on which it is filed.
- (5) On the disposal of the appeal, the Commissioner (Appeals) shall communicate the order passed by him to the appellant, the adjudicating authority and the Commissioner of Customs.

(B) APPELLATE TRIBUNAL (SECTION 129)

- (1) The Central Government shall constitute an Appellate Tribunal to be called the Customs, Excise and Service Tax Appellate Tribunal consisting of as many judicial and technical members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act.
- (2) A judicial member shall be a person who has for at least ten years held a judicial office in the territory of India or who has been a member of the Indian Legal Service and has held a post in Grade I of that service or any equivalent or higher post for at least three years, or who has been an advocate for at least ten years.

Explanation: For the purposes of this sub-section—

- (i) in computing the period during which a person has held judicial office in the territory of India, there shall be included any period, after he has held any judicial office, during which the person has been an advocate or has held the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law;
 - (ii) in computing the period during which a person has been an advocate, there shall be included any period during which the person has held a judicial office or the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law after he became an advocate.
- (2A) A technical member shall be a person who has been a member of the Indian Customs and Central Excise Service, Group A, and has held the post of Commissioner of Customs or Central Excise or any equivalent or higher post for at least three years.
- (3) The Central Government shall appoint—
- (a) a person who is or has been a Judge of a High Court; or
 - (b) one of the members of the Appellate Tribunal, to be the President thereof.
- (4) The Central Government may appoint one or more members of the Appellate Tribunal to be the Vice-President, or, as the case may be, Vice-Presidents, thereof.
- (4A) Omitted by Finance Act, 2003.
- (5) Vice-President shall exercise such of the powers and perform such of the functions of the President as may be delegated to him by the President by a general or special order in writing.

APPEALS TO THE APPELLATE TRIBUNAL (SECTION 129A)

- (1) Any person aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order:
- (a) a decision or order passed by the Commissioner of Customs as an adjudicating authority;
 - (b) an order passed by the Commissioner (Appeals) under Section 128A;
 - (c) an order passed by the Board or the Appellate Commissioner of Customs under Section 128, as it stood immediately before the appointed day;
 - (d) an order passed by the Board or the Commissioner of Customs, either before or after the appointed day, under Section 130, as it stood immediately before that day:

Provided that no appeal shall lie to the Appellate Tribunal and the Appellate Tribunal shall not have jurisdiction to decide any appeal in respect of any order referred to in clause (b), if such order relates to:

- (a) any goods imported or exported as baggage;
- (b) any goods loaded in a conveyance for importation into India, but which are not unloaded at their place of destination in India, or so much of the quantity of such goods as has not been unloaded at any such destination if goods unloaded at such destination are short of the quantity required to be unloaded at that destination;
- (c) payment of drawback as provided in Chapter X, and the rules made thereunder;

Provided further that the Appellate Tribunal may, in its discretion, refuse to admit an appeal in respect of an order referred to in clause (b) or clause (c) or (d) where:

- (i) the value of the goods confiscated without option having been given to the owner of the goods to pay a fine in lieu of confiscation under Section 125; or
 - (ii) in any disputed case other than a case where the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or
 - (iii) the amount of fine or penalty determined by such order, does not exceed Fifty thousand rupees.
- (1A) Every appeal against any order of the nature referred to in the first proviso to Sub-section (1), which is pending immediately before the commencement of Section 40 of the Finance Act, 1984, before the Appellate Tribunal and any matter arising out of or connected with such appeal and which is so pending shall stand transferred on such commencement to the Central Government under Section 129DD as if such appeal or matter were an application or a matter arising out of an application made to it under that section.
- (1B) The Board may, by notification in the Official Gazette constitute such committees as may be necessary for the purpose of this Act, consisting of two Chief Commissioners or Commissioners of Customs.
- (2) The Committee of Commissioners of Customs may, if it is of opinion that an order passed by the Appellate Commissioner of Customs under Section 128 as it stood immediately before the appointed day, or by the Commissioner (Appeals) under Section 128A, is not legal or proper, direct the proper officer to appeal on its behalf to the Appellate Tribunal against such order.
- Provided that where the Committee of Commissioners of Customs differs in its opinion regarding the appeal against the order of the Commissioner (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Chief Commissioner of Customs who shall, after considering the facts of the order, if is of the opinion that the order passed by the Commissioner (Appeals) is not legal or proper, direct the proper officer to appeal to the Appellate Tribunal against such order.
- Explanation:* For the purposes of this sub-section, "jurisdictional Chief Commissioner" means the Chief Commissioner of Customs having jurisdiction over the adjudicating authority in the matter.
- (3) Every appeal under this section shall be filed within three months from the date on which the order sought to be appealed against is communicated to the Commissioner of Customs, or as the case may be, the other party preferring the appeal.
- (4) On receipt of notice that an appeal has been preferred under the section, the party against whom the appeal has been preferred may, notwithstanding that he may not have appealed against such order or any part thereof, file, within forty-five days of the receipt of the notice, a memorandum of cross-objections verified in such manner as may be specified by rules made in this behalf against any part of the order appealed against and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in Sub-section (3).
- (5) The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period referred to in Sub-section (3) or Sub-section (4), if it is satisfied that there was sufficient cause for not presenting it within that period.
- (6) An appeal to the Appellate Tribunal shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf and shall, irrespective of the date of demand of duty and interest or of levy of penalty in relation to which the appeal is made, be accompanied by a fee of:
- (a) where the amount of duty and interest demanded and penalty levied by any officer of customs

- in the case to which the appeal relates is five lakh rupees or less, one thousand rupees;
- (b) where the amount of duty and interest demanded and penalty levied by any officer of customs in the case to which the appeal relates is more than five lakh rupees, but not exceeding fifty lakh rupees, five thousand rupees;
 - (c) where the amount of duty and interest demanded and penalty levied by any officer of customs in the case to which the appeal relates is more than fifty lakh rupees, ten thousand rupees:
- Provided that no such fee shall be payable in the case of an appeal referred to in Sub-section (2) or a memorandum of cross-objections referred to in Sub-section (4).
- (7) Every application made before that Appellate Tribunal,-
- (a) in an appeal for grant of stay or for rectification of mistake or for any other purpose; or
 - (b) for restoration of an appeal or an application, shall be accompanied by a fee of five hundred rupees.

ORDERS OF APPELLATE TRIBUNAL (SECTION 129B)

- (1) The Appellate Tribunal may, after giving the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or annulling the decision or order appealed against or may refer the case back to the authority which passed such decision or order with such directions as the Appellate Tribunal may think fit, for a fresh adjudication or decision, as the case may be, after taking additional evidence, if necessary.
 - (2) The Appellate Tribunal may, at any time within six months from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it under Sub-section (1) shall make such amendments if the mistake is brought to its notice by the Commissioner of Customs or the other party to the appeal:
- Provided that an amendment which has the effect of enhancing the assessment or reducing a refund or otherwise increasing the liability of the other party shall not be made under this sub-section, unless the Appellate Tribunal has given notice to him of its intention to do so and has allowed him a reasonable opportunity of being heard.
- (2A) The Appellate Tribunal shall, where it is possible to do so, hear and decide every appeal within a period of three years from the date on which such appeal is filed:
- Provided that where an order of stay is made in any proceeding relating to an appeal filed under Sub-section (1) of Section 129A, the Appellate Tribunal shall dispose of the appeal within a period of one hundred and eighty days from the date of such order:
- Provided further that if such appeal is not disposed of within the period specified in the first proviso, the stay order shall, on the expiry of that period, stand vacated.
- If such appeal is not disposed of within the period specified, the stay order shall on the expiry of that period, stand vacated.
- If the appeal is not disposed of within the period specified in the above, the Appellate Tribunal may on an application made in this behalf by a party and on being satisfied that delay in disposing of the appeal is not attributable to such party, extend the period of stay to such further period, as it thinks fit, not exceeding 185 days and in case the appeal is not disposed of within 365 days, the stay order shall stand vacated.
- (3) The Appellate Tribunal shall send a copy of every order passed under this section to the

Commissioner of Customs and the other party to the appeal.

- (4) Save as otherwise provided in Section 130 or Section 130E, order passed by the Appellate Tribunal on appeal shall be final.

PROCEDURE OF APPELLATE TRIBUNAL (SECTION 129C)

- (1) The powers and functions of the Appellate Tribunal may be exercised and discharged by Benches constituted by the President from amongst the members thereof.
- (2) Subject to the provisions contained in Sub-section (4), a Bench shall consist of one judicial member and one technical member.
- (3) Omitted by Finance Act, 1995.
- (4) The President or any other member of the Appellate Tribunal authorised in this behalf by the President may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member where —
 - (a) the value of the goods confiscated without option having been given to the owner of the goods to pay a fine in lieu of confiscation under Section 125; or
 - (b) in any disputed case other than a case where the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or
 - (c) the amount of fine or penalty involved; does not exceed 50 Lakh rupees.
- (5) If the members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority, if there is a majority; but if the members are equally divided, they shall state the point or points on which they differ and make a reference to the President who shall either hear the point or points himself or refer the case for hearing on such point or point by one or more of the other members of the Appellate Tribunal and such point or points shall be decided according to the opinion of the majority of these members of the Appellate Tribunal who have heard the case, including those who first heard it.
- (6) Subject to the provisions of this Act, the Appellate Tribunal shall have power to regulate its own procedure and the procedure of the Benches thereof in all matters arising out of the exercise of its powers or of the discharge of its functions, including the places at which the Benches shall hold their sittings.
- (7) The Appellate Tribunal shall, for the purposes of discharging its functions, have the same powers as are vested in a court under the Code of Civil Procedure, 1908 (5 of 1908) when trying a suit in respect of the following matters, namely:
 - (a) discovery and inspection;
 - (b) enforcing the attendance of any person and examining him on oath;
 - (c) compelling the production of books of account and other documents; and
 - (d) issuing commissions.
- (8) Any proceedings before the Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of Sections 193 and 228 and for the purpose of Section 196 of the Indian Penal Code

(45 of 1860), and the Appellate Tribunal shall be deemed to be a Civil Court for all the purpose of Section 195 and Chapter XXVII of the Code of Criminal Procedure, 1973 (2 of 1974).

POWERS OF COMMITTEE OF CHIEF COMMISSIONERS OF CUSTOMS OR COMMISSIONERS OF CUSTOMS TO PASS CERTAIN ORDERS (SECTION 129D)

- (1) The Committee of Chief Commissioners may, of its own motion, call for and examine the record of any proceeding in which a Commissioner of Customs as an adjudicating authority has passed any decision or order under this Act for the purpose of satisfying itself as to the legality or propriety of any such decision or order and may, by order, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order as may be specified by the Committee of Chief Commissioners in its order.

Provided that where the Committee of Chief Commissioners of Customs differs in its opinion as to the legality or propriety of the decision or order of the Commissioner of Customs, it shall state the point or points on which it differs and make a reference to the Board. After considering the facts of the decision or order passed by the Commissioner of Customs, if the board is of the opinion that the decision or order passed by the Commissioner of Customs is not legal or proper, it may direct such Commissioner or any other Commissioner to make an appeal to the Appellate Tribunal for the determination of such points arising out of the decision or order.

- (2) The Commissioner of Customs may, of his own motion, call for and examine the record of any proceedings in which an adjudicating authority subordinate to him has passed any decision or order under this Act for the purpose of satisfying himself as to the legality or propriety of any such decision or order and may, by order, direct such authority to apply to the Commissioner (Appeals) for the determination of such points arising out of the decision or order as may be specified by the Commissioner of Customs in his order.
- (3) Every order under Sub-section (1) or Sub-section (2), shall be made within a period of three months from the date of communication of the decision or order of the adjudicating authority.
- (4) Where in pursuance of an order under Sub-section (1) or Sub-section (2), the adjudicating authority or any officer of customs authorised in this behalf by the Commissioner of Customs, makes an application to the Appellate Tribunal or the Commissioner (Appeals) within a period of three months from the date of communication of the order under Sub-section (1) or Sub-section (2) to the adjudicating authority, such application shall be heard by the Appellate Tribunal or the Commissioner (Appeals), as the case may be, as if such application were an appeal made against the decision or order of the adjudicating authority and the provisions of this Act regarding appeals, including the provisions of Sub-section (4) of Section 129A shall, so far as may be, apply to such application.

REVISION BY CENTRAL GOVERNMENT (SECTION 129DD)

- (1) The Central Government may, on the application of any person aggrieved by any order passed under Section 128A, where the order is of the nature referred to in the first proviso to Sub-section (1) of Section 129A, annul or modify such order.

Provided that the Central Government may in its discretion refuse to admit an application in respect of an order where the amount of duty or fine or penalty, determined by such order does not exceed five thousand rupees.

Explanation: For the purposes of this sub-section. "Order passed under Section 128A" includes an order passed under that section before the commencement of Section 40 of the Finance Act, 1984,

against which an appeal has not been preferred before such commencement and could have been, if the said section had not come into force, preferred after such commencement, to the Appellate Tribunal.

- (1A) The Commissioner of Customs may, if he is of the opinion that an order passed by the Commissioner (Appeals) under Section 128A is not legal or proper direct the proper officer to make an application on his behalf to the Central Government for revision of such order.
- (2) An application under Sub-section (1) shall be made within three months from the date of the communication to the applicant of the order against which the application is being made:

Provided that the Central Government may, if it is satisfied that the applicant was prevented by sufficient cause from presenting the application within the aforesaid period of three months, allow it to be presented within a further period of three months.

- (3) An application under Sub-section (1) shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf and shall be accompanied by a fee of:
 - (a) two hundred rupees, where the amount of duty and interest demanded, fine or penalty levied by an officer of customs in the case to which the application relates is one lakh rupees or less;
 - (b) one thousand rupees, where the amount of duty and interest demanded, fine or penalty levied by an officer of customs in the case to which the application relates is more than one lakh rupees;

Provided that no such fee shall be payable in the case of an application referred to in Sub-section (1A).

- (4) The Central Government may, of its own motion, annul or modify any order referred to in Sub-section (1).
- (5) No order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value shall be passed under this 'section—
 - (a) in any case in which an order passed under Section 128A has enhanced any penalty or fine in lieu of confiscation or has confiscated goods of greater value, and
 - (b) in any other case, unless the person affected by the proposed order has been given notice to show cause against it within one year from the date of the order sought to be annulled or modified.
- (6) Where the Central Government is of opinion that any duty of customs has not been levied or has been short-levied, no order levying or enhancing the duty shall be made under this section unless the person affected by the proposed order is given notice to show cause against it within the time limit specified in Section 28.

APPEAL TO SUPREME COURT (SECTION 130E)

An appeal shall lie to the Supreme Court from—

- (a) any judgment of the High Court delivered in any case which, on its own motion or on an oral application made by or on behalf of the party aggrieved, immediately after the passing of the judgment, the High Court certifies to be a fit one for appeal to the Supreme Court; or
- (b) any order passed before the establishment of the National Tax Tribunal by the Appellate Tribunal relating, among other things, to the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment.

HEARING BEFORE SUPREME COURT (SECTION 130F)

- (1) The provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the Supreme Court shall, so far as may be, apply in the case of appeals under Section 130E as they apply in the case of appeals from decrees of a High Court:

Provided that nothing in this Sub-section shall be deemed to affect the provisions of Section 131.

- (2) The costs of the appeal shall be in discretion of the Supreme Court.
- (3) Where the judgment of the High Court is varied or reversed in the appeal effect shall be given to the order of the Supreme Court in the case of a judgment of the High Court.

DEPOSIT, PENDING APPEAL, OF DUTY AND INTEREST DEMANDED OR PENALTY LEVIED (SECTION 129E)

Where in any appeal under this Chapter, the decision or order appealed against relates to any duty and interest demanded in respect of goods which are not under the control of the customs authorities or any penalty levied under this Act, the person desirous of appealing against such decision or order shall, pending the appeal, deposit with the proper officer, the duty and interest demanded or the penalty levied:

Provided that where in any particular case, the Commissioner (Appeals) or the Appellate Tribunal is of opinion that the deposit of duty and interest demanded or penalty levied would cause undue hardship to such person, the Commissioner (Appeals) or, as the case may be, the Appellate Tribunal, may dispense with such deposit subject to such conditions as he or it may deem fit to impose so as to safeguard the interests of revenue.

Provided further that where an application is filed before the Commissioner (Appeals) for dispensing with the deposit of duty and interest demanded or penalty levied under the first proviso, the Commissioner (Appeals) shall, where it is possible to do so, decide such application within thirty days from the date of its filing.

INTEREST ON DELAY PAYMENT OF REFUND (SECTION 129EE)

Where an amount deposited by the appellant in pursuance of an order passed by the Commissioner (Appeals) or the appellate authority, under the first proviso to section 129E, is required to be refunded consequent upon the order of the appellate authority and such amount is not refunded within three months from the date of communication of such order to the adjudicating authority, unless the operation of the order of the appellate authority is stayed by a superior court or tribunal, there shall be paid to the appellant interest at the rate specified in section 27A after the expiry of three months from the date of communication of the order of the appellate authority, till the date of refund of such amount.

[Section 130, 130A, 130B, 130C and 130D are omitted by National Tax Tribunal Act, 2005 with effect from a date yet to be notified].

SUMS DUE TO BE PAID NOTWITHSTANDING REFERENCE, ETC. (SECTION 131)

Notwithstanding that a reference has been made to the High Court or the Supreme Court or an appeal has been preferred to the Supreme Court, under this Act before the commencement of the National Tax Tribunal Act, 2005, sums due to the Government as a result of an order passed under Sub-section (1) of Section 129B shall be payable in accordance with the order so passed.

EXCLUSION OF TIME TAKEN FOR COPY (SECTION 131A)

In computing the period of limitation, specified for an appeal or application under this Chapter, the day on

which the order complained of was served, and if the party preferring the appeal or making the application was not furnished with a copy of the order when the notice of the order was served upon him, the time requisite for obtaining a copy of such order shall be excluded.

TRANSFER OF CERTAIN PENDING PROCEEDINGS AND TRANSITIONAL PROVISIONS (SECTION 131B)

- (1) Every appeal which is pending immediately before the appointed day before the Board under Section 128, as it stood immediately before that day, and any matter arising out of or connected with such appeal and which is so pending shall stand transferred on that day to the Appellate Tribunal and the Appellate Tribunal may proceed with such appeal or matter from the stage at which it was on that day:

Provided that the appellant may demand that before proceeding further with that appeal or matter, he may be re-heard.
- (2) Every proceeding which is pending immediately before the appointed day before the Central Government under Section 131, as it stood immediately before that day, and any matter arising out of or connected with such proceeding and which is so pending shall stand transferred on that day to the Appellate Tribunal and the Appellate Tribunal may proceed with such proceeding or matter from the stage at which it was on that day as if such proceeding or matter were an appeal filed before it:

Provided that, if any such proceeding or matter relates to an order where—

 - (a) the value of the goods confiscated without option having been given to the owner of the goods to pay a fine in lieu of confiscation under Section 125; or
 - (b) in any disputed case, other than a case where the determination of any question having a relation to the rate of duty of customs or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or
 - (c) the amount of fine or penalty determined by such order, does not exceed ten thousand rupees, such proceeding or matter shall continue to be dealt with by the Central Government as if the said Section 131 had not been substituted:

Provided, further that the applicant or the other party may make a demand to the Appellate Tribunal that before proceeding further with that proceeding or matter, he may be re-heard.
- (3) Every proceeding which is pending immediately before the appointed day before the Board or the Commissioner of Customs under Section 130, as it stood immediately before that day, and any matter arising out of or connected with such proceeding and which is so pending shall continue to be dealt with by the Board or the Commissioner of Customs, as the case may be, as if the said section had not been substituted.
- (4) Any person who immediately before the appointed day was authorised to appear in any appeal or proceeding transferred under Sub-section (1) or Sub-section (2) shall, notwithstanding anything contained in Section 146A, have the right to appear before the Appellate Tribunal in relation to such appeal or proceeding.

APPEAL NOT TO BE FILED IN CERTAIN CASES (SECTION 131BA)

Section 131BA provides that notwithstanding the fact that no appeal, application, revision or reference has been filed by the Commissioner of customs against any decision or order passed under the provisions of the act pursuant to the order or instruction or direction issued by the board. Then—

- (a) no person, being a party in appeal, application, revision or reference shall contend that the

commissioner of customs has acquiesced in the decision on the disputed issue by not filing appeal, application, revision or reference; and

- (b) the appellate tribunal or court hearing an appeal, application, revision or reference shall have regard to the circumstances under which the appeal, application, revision or reference was not filed by the commissioner of customs in pursuance of order or instruction or direction by the board.

LESSON ROUND UP

- Under this lesson we have discussed the remedies available for the disputes arises under the Customs and Excise Law.
- To give binding rulings in advance on Central Excise, Customs and Service tax matters pertaining to an investment venture in India. Authority for Advance Ruling was set up.
- The procedure for obtaining advance ruling is simple, inexpensive and transparent.
- Settlement commission also provides quick and easy settlement of tax disputes involving high revenue stake. The specified person can make application before the settlement commission.
- Appeal against the orders of Central Excise Officers. Customs officers can be made to the Central Excise (Appeals) or Customs (Appeals) then against these orders appeal can be made before the Appellate Tribunals and then before the High Court and Supreme Court.

SELF TEST QUESTIONS

1. What Appellate Scheme has been provided under the Central Excise?
2. What is the procedure for filing Appeal before Commissioner (Appeals)?
3. Discuss the circumstances under which Department may order for re-opening of its original orders/decisions and the procedure it has to follow in this regard.
4. What is the mechanism provided in the Customs Act for adjudication of disputes between the assessee and the department?
5. When can an appeal be filed before the Commissioner (Appeals)?
6. What is Customs, Excise and Service Tax Appellate Tribunal (CESTAT)?
7. What are the matters in respect of which an appeal can be made before CESTAT?
8. What is the procedure of filing and disposal of stay petitions under CESTAT Rules?
9. What are the revisionary powers of the Central Government on adjudicated matters under Customs Act?
10. When does an appeal lie before Supreme Court under appellate provisions of Customs Act, 1962?
11. What is the procedure of filing a revision application to the Central Government under appellate provisions of Customs Act?
12. Who can act as an 'authorised representative' in adjudication of disputes and appeals under the Customs Act and Rules?
13. Explain briefly the concept of Settlement Commission.
14. What provisions are made under the Customs Act, 1962 to deal with various kinds of offences of Customs?

15. Can a mere preparation towards an act of offence of Customs laws be punished under the Act? State the circumstances.
16. What are the provisions under Customs Act, regarding the power of Court to publish name, place of business, etc. of persons convicted under the Act?
17. When can a Court take cognizance of an offence committed under the Customs Act, 1962?
18. What are the provisions under the Customs Act, with regard to use of Statements, and documents as evidence during prosecution for an offence of Customs?
19. What powers the officers of Customs have in respect of recovery of sums due to the Government on account of duties of Customs?
20. When can an import of material be cleared without payment of duty leviable thereon?
21. State the requirements laid down under the Customs Act with regard to the 'eligibility to function' as an import or export agent.
22. Who is an 'authorised representative' for the purpose of appearance before an officer of Customs or Customs Tribunal.

SUGGESTED READINGS

- (1) Customs Law Manual — *R. K. Jain*
- (2) Indirect Taxes—Law and Practice — *V.S. Datey*

Lesson 8

Promissory Estoppel in Fiscal Laws, Tax Planning and Tax Management

LESSON OUTLINE

- Meaning of Doctrine of Promissory Estoppel
- Requirements of Promissory Estoppel
- Promissory Estoppel in Fiscal Laws
- Limitation of the Doctrine
- Tax Planning
- Tax Planning under Excise law
- Tax planning under Customs Act
- Lesson Round Up
- Self Test Questions

LEARNING OBJECTIVES

This lesson is divided into two parts i.e. promissory estoppel in fiscal laws and Tax planning and management with respect to indirect taxes. 'Promissory Estoppel', as an equitable principle, has been in vogue in judicial systems for long. Intended to counter the evading tendencies and insist upon parties to perform the promises made, the principle of promissory estoppel relieves the parties aggrieved from such breach of promises. Here, we will discuss the applicability of Doctrine of promissory estoppel.

Tax planning in indirect taxes is thrust area in the business world. Indirect taxes constitute major portion of cost and therefore it is necessary that proper tax management shall be complied with. Indirect taxes are ruled by complex regulations and are often changing. By successfully managing indirect tax requirements of a business, the business's profitability can be protected and also cash flow needs. Professionals like Company Secretaries can provide their services in managing the tax compliances and thereby reducing the administration cost.

After completion of this lesson, the students will understand:

- What is promissory estoppel
- Applicability of doctrine of promissory estoppel under Indirect taxes
- Tax planning under indirect taxes

Indirect taxes include customs duties, excise laws and taxes on consumption, such as Value Added Tax (VAT) and Goods and Services Tax (GST). These taxes apply to every stage of the supply chain. Managing these taxes to reduce costs and avoid errors that lead to penalties and business disruption is crucial to maintain profits.

MEANING OF DOCTRINE OF PROMISSORY ESTOPPEL

Promissory estoppel is a common law doctrine used by courts to enforce promises that have been made and subsequently relied upon. Promissory estoppel usually comes into play when there is no formal contract, but the parties involved have nevertheless acted as if there was one. Courts use the doctrine in these circumstances to impose a contract on the agreement, usually in the interest of fairness.

In common language, "promissory" means "related to a promise," and "estoppel" is a legal term that essentially means an enforced bar or ban. Judges use the doctrine to ban one person from going back on a promise. Seen from a different angle, the doctrine is a tool to enforce promises, effectively requiring both parties to do the things they said they would.

The doctrine of Promissory Estoppel has its genesis in the law of equity and being closely related to various schemes for allowing tax concessions to certain new industrial units set up within specified time or in specified places, it has become very relevant in fiscal legislations particularly in Sales-tax, Excise and Custom duty disputes. The doctrine is not limited in its application only to defence but also in a cause of action. This concept and its applicability have often been agitated before the court in the context of sales tax exemption. The gist of equity lies in the fact that one party has by his conduct or representation led the other to alter his position. If injustice can be avoided only by enforcement of the promise, it is a case of estoppel.

In *Delhi Cloth and General Mills Ltd. v. Union of India*, it was held that:

"All that is now required is that the party asserting the estoppel must have acted upon the assurance given to him. Must have relied upon the representation made to him. It means, the party has changed or altered the position by relying on the assurance or representation. The alteration of position by the party is the only indispensable requirement of the doctrine. It is not necessary to prove further any damage, detriment or prejudice to the party asserting the estoppel.

The doctrine of estoppel has its origin in principles of Equity. It was defined under Section 115 of the Evidence Act, 1872 as follows;

"When one person has, by his declaration, act or omission, intentionally caused or permitted another person to believe a thing to be true and to act upon such belief, neither he nor his representative shall be allowed, in any suit or proceeding between himself and such person or his representative, to deny the truth of that thing."

The estoppel operates as a legal protection to the person who acts in good faith on the basis of express or implied conduct of others and suffers damage.

The Doctrine of Promissory Estoppel is an equitable doctrine evolved to avoid injustice and it falls in the sphere of neither contract nor estoppel. This principle is commonly invoked in common law in case of breach of contract or against a Government. The doctrine is popularly called as Promissory Estoppel, Equitable Estoppel, Quasi Estoppel and New Estoppel. It can be said that if the Government in India makes a promise to any person and the promise is not inconsistent with the law of the land and is not against public interest, then afterwards it cannot refuse to abide by its promise.

An example of promissory estoppel is where 'A' promises 'B' that he would not enforce his legal rights and B acted and relied on it without giving any consideration, equity would not allow A to renege on his promise to B.

REQUIREMENTS OF PROMISSORY ESTOPPEL

- (1) There is a pre-existing contractual relationship.

- (2) One party to that contract makes a clear promise that they will not fully enforce their legal rights (under that contract).
- (3) The promisor intends that promise be relied upon and promisee does in fact rely upon it.
- (4) It would be inequitable for promisor to go back on (resile from) their promise.

Promissory estoppel is not limited only to cases where there is some contractual relationship or other pre-existing legal relationship between the parties. The principle can be applied even when the promise is intended to create legal relations or affect a legal relationship which will arise in future.

Promise need not be express; it can be implied from circumstances.

DOCTRINE OF PROMISSORY ESTOPPEL AND FISCAL LAWS

The doctrine of promissory estoppel has great significance in taxing statutes. It marches with the hypotheses that a promise given by the state is binding on the government in the following circumstances:

1. Where there is a clear and unequivocal promise knowing and intending that it would be acted upon by the promisee; and
2. By acting upon the promise by the promisee, it would be inequitable to allow the promisor to go back on the promise.

This is raised in tax matters, especially in Sales tax where the Government provides exemption from tax by means of tax holiday for a certain period say 5 years and withdraws the exemption before the expiry of 5 years.

The plea of promissory estoppel is on the ground that certain units have been established expecting the tax benefits and the withdrawal before the expiry has caused damage to them. Here, the units might be hit hard. They can go to the court of law against the Govt. under Doctrine of Estoppel. The doctrine was first introduced in *Hughes v. Metropolitan Rly. Co.*, 1877, Appeal case 439. Lord Cairns stated the doctrine in the following words :

“It is the first principle upon which all Courts of Equity proceed, that if parties who have entered into definite and distinct terms involving certain legal results afterwards by their own act or with their own consent enter upon a course of negotiation which has the effect of leading one of the parties to suppose that the strict rights arising under the contract will not be enforced, or will be kept in suspense, or held in abeyance, the person who otherwise might have enforced those rights will not be allowed to enforce them where it would be inequitable having regard to the dealings which have thus taken place between the parties”.

The doctrine of promissory estoppel is also known as equitable estoppel or quasi estoppel.

Courts on Promissory Estoppel

The courts while recognizing the principle of promissory estoppel as an instrument of equity remedy have consistently held that the ‘promissory estoppel plea’ fails where ‘public interest’ intervenes. That means, though a concession is extended for a fixed period by a notification or otherwise the same can be withdrawn in public interest in *Sales Tax Officer & Another v. M/s. Shree Durga Oil Mills* (1997) 7 SCALE, 726, the honourable Supreme Court held that a notification granting exemption of taxes can be withdrawn at any point of time. There can not be estoppel against any statute. Where it is in public interest, the court will not interfere because public interest must override any consideration of private loss or gain.

A leading authority on this subject is of the Supreme Court in *Motilal Padampat Sugar Mills Co Ltd. v State of Uttar Pradesh* (118 I.T.R. 326).

It was held that the government is susceptible to the operation of the doctrine in whatever area or field the promise is made: Contractual, administrative or statutory.

"The law may, therefore, now be taken to be settled as a result of this decision, that where the government makes a promise knowing or intending that it would be acted on by the promisee and, in fact, the promisee, acting in reliance on it, alters his position, the Government would be held bound by the promise and the promise would be enforceable against the Government at the instance of the promisee, notwithstanding that there is no consideration for the promise and the promise is not recorded in the form of a formal contract as required by Article 299 of the Constitution."

In *Sree Sales Corporation & Another v. U.O.I.* (1997) 3 SCC 398, it was held that where there was supervening public interest, the Govt. is free to change its stand and withdraw the exemption already granted. Recently, in *Sharma Transport v. Govt. of A.P. & Others* (2002) S.C., the Supreme Court observed "one such reason for changing its policy decision can be resource crunch and the loss of public revenue. There is preponderance of judicial opinion that to invoke the doctrine of promissory estoppel, clear sound and positive foundation must be laid in the petition itself by the party invoking the doctrine and that bold expressions without any supporting material to the effect that the doctrine is attracted because the party invoking the doctrine has altered his position relying on the assurance of the Govt. would not be sufficient to press into aid the doctrine. 'Doctrine of promissory estoppel' has been evolved by Courts on the principles of equity, to avoid injustice.

In the above case, the appellants were operators of tourist buses originating from the State of Karnataka and running their buses in adjacent states including the state of A.P.

The vehicles of the appellants were covered by tourist vehicle permits by virtue of which, their vehicles were authorised to ply in certain contiguous states also.

The Central Government formulated policies in the matter of concessions to be extended to tourist vehicles. Based on the directive of the Central Govt. an order was issued on 1st July, 1995 conferring the benefits of a concessional rate of tax to tourist operators. But on 5th June 2000, the State Govt. issued a notification under A.P. Motor Vehicles Taxation Act, 1963 cancelling the earlier order of 1995. The operators after losing the High Court of A.P. filed an appeal before the Supreme Court. The Contentions before the apex Court were — that the directives of the Central Govt. were binding on the State Govt. and that the withdrawal of tax concession is illegal. They also contended that under doctrine of promissory estoppel, a concession extended by the Govt. could not be withdrawn.

But the Supreme Court rejects the pleas and dismissed the appeal stating that the state of A.P. is justified in withdrawing the benefits in public interest. Also held that the doctrine of promissory estoppel is not applicable in the case.

Thus we can conclude that the doctrine of promissory estoppel is a valid proposition but it will be disallowed by courts when the withdrawal of tax benefit by the Govt. is to save the larger interests of the public.

As can be seen from the analysis of the cases above, the concept of Promissory Estoppel has assumed considerable significance in sales tax law. Many a time the State Governments with a view to giving a spur to industrial development in the State give sales tax exemptions. Subsequently, State Governments may either withdraw the exemption notification or introduce certain restrictive covenants. This becomes necessary in view of the loss of the revenue to the State Government, as a result of the sales tax exemption granted earlier. In such a situation, whether the State has to be held bound to the representation made earlier to the trade or not depends upon whether the exemption was for a particular period or whether the industry has altered its position in the light of the notification etc. It is once again reiterated that if a State Government

issues a general exemption notification with no reference to any period of time such exemption may be amended or varied at any time. There would be no question of any promissory estoppel in such cases. But where the State Government hold out that exemption from sales tax would accrue for a given period of time of three years or five years than promissory estoppel would be applied.

CASE STUDIES

In the recent past various area-based Notifications had been issued by the Ministry of Finance whereby exemption from the payment of excise duty was granted to the assessees upon fulfillment of the conditions specified therein. Development of identified backward areas and promotion of industrial activity therein being the underlying premise, these Notifications provided exemption for specified periods to the assessees complying with the prescribed conditions. North-East, Uttranchal, Himachal Pradesh, Sikkim, Jammu & Kashmir were some of these areas wherefore the Notifications were issued granting the exemption of excise duty.

Lured by these promises on the part of the Central Government waiving the collection of excise duty, many industrial and production houses established/relocated their manufacturing units in these areas. The establishment or relocation, however, was not without cost. Non-availability of skilled man-power, lack of natural or industrial resources required for manufacturing processes, absence of logistics network, etc. posed considerable obstacles to the establishment of manufacturing facilities from these units, leading to increase in operational costs and delay of break-even points.

However, comforted by the Government's promise to exempt the excise duties for the specified period, the business houses continued to build their units in these areas expecting returns in the long-term vision of affairs. The losses in the initial years on account of these incorporation costs were reluctantly absorbed expecting to recover them in form of exempted excise duties.

In this scenario, can the Government rightfully have recalled its decision to exempt the areas during the continuation of the holiday period? Can the Government backtrack on its promise as evidenced in the Notifications? Can the Government, before the expiry of the exemption period, amend the Notification to levy excise duties? These are critical questions facing the Central Excise paradigm today for the Central Government has in fact, on more than one occasion, amended these exemption Notifications to levy duties of excise on some or all goods. Notification No. 18/2008-CE has amended the parent Notification No. 33/1999-CE exempting payment of excise duties in various areas of Assam. Similarly Notification No. 21/2007-CE and Notification No. 19/2008-CE have amended parent Notification No. 56/2003-CE and Notification No. 56/2002-CE which provided for exemption for areas in Sikkim and Jammu & Kashmir respectively. These amending Notifications have restricted the availability of the exemptions extended under the parent Notifications and thus varied the originally specified conditions.

The affected manufacturing units would, naturally, find these amendments prejudicial to their operations and grossly offending the original promise. The emotional yet precarious arguments against such withdrawal of exemptions nonetheless, the thrust of the matter is whether the affected units can get their grievances redressed. Only two solutions seem probably in such a scenario; either the industrial units make representations to the Ministry and secure a withdrawal of these amending Notifications or to get their claims enforced in courts of law. Neither of the scenario inspire confidence for in the former case the attitude of the Ministry to limit the exemptions is evident in light of the amending Notifications and in the case of latter, Section 21 of the General Clauses Act, 1893 unequivocally declares that the 'power to make' includes the 'power to add to, amend, vary or rescind orders, rules or byelaws' and thus the power to amend the parent Notifications vests unshakably in the Central Government.

Does this imply that the assessees who have established their units in these notified areas in pursuance of the promise of the Government are left to suffer to its whims and surmises? Is there any forum where these

assessees can get their grievance addressed or is it a shut case against their face? Would the entire infrastructural developmental expenditure incurred by these units to promote the backward areas come to haunt against their profitability with no respite from the government? Considering the categorical intent of the Central Government, as evident from the amending Notifications, and given the magnitude of powers vested therein to issue and rescind Notifications, the issue does seem to favour the revenue and against the assessee. A solemn resolve of a legal practitioner to get these genuine grievances redressed, therefore, would require nothing short of a fire-fight and it is in this backdrop that like a silver lining in a gray cloud, the doctrine of promissory estoppel seems to show the light of the day.

The Hon'ble Supreme Court of India dealt with this "question of considerable importance in the field of public law" in the case of *Motilal Padampat Sugar Mills Ltd.* (decision dated 12.12.1978). The precise issue before the Court then was "How far and to what extent is the State bound by the doctrine of promissory estoppel". The Court was required to assess the legality of the withdrawal of exemption by the State of Uttar Pradesh in a factual milieu wherein the Sugar Mill was assured of sales tax exemption for three years upon establishment of a 'vanaspati plant' by the Government and thereupon the Sugar Mill had borrowed money from various financial establishments and acted upon the establishment of the said plant. The Hon'ble Apex Court declared categorically that the State Government was bound by the doctrine of Promissory Estoppel and therefore the exemption promised was duly restored back to the aggrieved Sugar Mill.

The decision in *Motilal Padampat* serves a world of good in these critical times to the units suffering from the withdrawal of exemptions under the amending Notifications, however, not without a disclaimer. Since the decision in *Motilal Padampat* a lot of water has flown and the courts have not always been too impressed by the argument of the Government not being able to change the ground realities in the light of the changed economic scenarios and the demands for unbridled continuation of tax exemptions. In a number of instances the Hon'ble Supreme Court itself has declared the inapplicability of the doctrine in tax matters. While the Court approved the application of the doctrine in the case of *MRF Ltd.* (Civil Appeal No. 1610/2006), the decision in the similar circumstances in *R. C. Tobacco* (Civil Appeal No. 881- 896/2004) reflects its apathetic attitude in similar situation therein.

LIMITATION OF THE DOCTRINE

1. Since the doctrine of promissory estoppel is an equitable doctrine, it must yield when the equity so requires. But it is only if the court is satisfied, on proper and adequate material placed by the government, that overriding public interest requires that the government should not be held bound by the promise but should be free to act unfettered by it, that the court would refuse to enforce the promise against the government.
2. No representation can be enforced which is prohibited by law in the sense that the person or the authority making the representation or promise must have the power to carry out the promise.

If the power is there, then subject to the preconditions and limitations noted earlier, it must be exercised.

Thus, if the statute does not contain a provision enabling the Government to grant exemption, it would not be possible to enforce the representation against the Government, because the Government cannot be compelled to act contrary to the statute. But if the statute confers power on the Government to grant the exemption, the Government can legitimately be held bound by its promise to exempt the promisee from payment of any tax.

TAX PLANNING

Tax planning exercise needs to be undertaken with great amount of care and discretion. It should not border

on evasion nor should it merely be a device to circumvent the letter of law. In this context the Supreme Court's Judgements in *Mc Dowel and Company Ltd. v. Commercial Tax Officer* 1985, 5, ECC 259 was also studied in full text. This judgment signaled a departure from the West Minster Principle upon which most of the tax planning used to be founded and which for long had the judicial blessing. But the winds have changed since and in England the West Minster Principle has been given a go by. The Mc Dowel's judgement is a vindication of judicial attitude currently prevailing in England on the use of certain devices to avoid proper incidence of tax.

A trader or a Business entity need not be complacent in regard to payment of indirect taxes, for the simple reason that these are passed on to the consumers. It would only be a reiteration to say that tax planning is as much relevant and important in indirect taxes as it is in direct taxes.

The approach of tax planning has been to give a very rudimentary idea of tax planning vis-à-vis indirect taxes. No attempt has been made to repeat and elaborate discussions on various case laws concerning Excise, Customs and Sales Tax. The presentation is only skeletal and indicative of the broad contours of tax planning.

CUSTOMS ACT AND TAX PLANNING

Customs Act concerns Import and Export of Goods and restrictions and regulations relating thereto. Every importer or exporter and every buyer from such importer for instance, are interested in customs duty planning. For an importer, the tax planning centers round the classification of import goods and valuation of those goods. Improper classification of goods may lead to higher incidence of Customs Duty. On the other hand, even a proper and appropriate classification may not be a ground for feeling relaxed. Because even after correct classification, the valuation of Import of goods may be high pitched with the result the absolute incidence of customs duty would be much more than what it ought to have been. Importers therefore have to pay special attention to problems of classification and valuation of imported goods.

As regards valuation under the Customs law, besides the statutory provisions there are Customs Valuation Rules also. Apart from these, a good amount of case law has developed on what items are to be added to the value of the goods and what items going to reduce the value of goods. A proper tax planning exercise would have to take into consideration these aspects.

(a) Customs Act and Classification of goods

Classification of imported goods is very significant because a wrong classification may lead to a very high incidence of Customs Duty. The importer has therefore to be fully convergent with principles of classification of goods.

Since the subject of taxation is "goods", the concept underlying the levy is required to be understood. It is not the personal opinion of an individual Officer or for that matter of the assessee with regard to the classification of the "goods", that governs the issue. There are certain well defined criteria laid down by judicial decisions, which are required to be kept in mind. We saw what happened in the fountain pens case. In the case of *V.V. Iyer v. Jasjit Singh* (AIR 1973 SC 194), the appellant, who carried on business of importing plantation and agricultural machinery and implements had imported certain parts of agricultural machinery known as express Battery Sprayers which were classified under SL. No: 74 (x) of Part V of the Import Tariff Schedule which related to "sprayers (other than power driven) and parts". The appellant's contention was that he held an import licence for import of goods falling under serial No. 74(vi) of the said part of the said Schedule which related to "Parts of power driven agricultural machinery", the goods imported (liquid containers) were parts of sprayers and the said serial no. 74(vi), permitted all kinds of spare parts of power driven agricultural machinery. The sprayers imported, according to the appellant, function normally with the help of power

driven pumps and functionally, therefore, what the appellant imported were, correctly falling within serial No. 74(vi). As discussed earlier, the Supreme Court, however, did not interfere with the conclusions arrived at by the customs authorities.

In doing so, the Supreme Court was reiterating its earlier decisions in *Collector of Customs, Madras v. K. Ganga Shetty* [AIR (1963) SC 1319], and *A.V. Venkateswaran v. A.S. Wadhwani*, (AIR (1961) SC 1506). In Ganga Shetty's case, the respondent had imported from Australia a quantity of oats which was described in the indent, contract and shipping documents as "standard feed -oats". The commodity imported consisted of oats in whole grain. The question related to the proper classification of goods. The controversy centered round the point whether the "feed - oats" fell within S.No. 42 or S.No. 32 of the relevant Import Trade Control Schedule. During the relevant period S.No. 42 read:

"Fodder, bran and pollards, for the import of which a Special import licence was necessary" while item 32 read:

"Grain, not elsewhere specified, including broken grain but excluding flour -

- (a) oats;
- (b) others;

for which a licence was required.

The customs department held that the goods fell under S. No. 32 and established a case of importation without a valid licence. The contention of the importer was that the "feed oats" fell under the item relating to "fodder" because he had imported the goods solely for feeding race horse, at Bangalore and in South India, oats was not used as human food but only as a feed for horses and in any case, he was misled regarding the correct classification by an affirmative answer he had received from the Deputy Chief Controller of Imports, Madras to whom he had made a reference as to whether the goods could be imported under O.G.L. In the High Court, the decision was in favour of the respondent on the ground that in the Court's view, that "oats" fell under item 42 relating to "fodder" and that the decision of lower authorities was always open for judicial review.

In appeal the Supreme Court however, held that the High Court was not right in interfering with the decision of the Customs authorities since their decision to treat it as falling under item 32 "could not be said to be a view on which no reasonable interpretation could be entertained". In other words, the Supreme Court felt that the 'conclusion or decision of the customs authorities was rationally supportable'.

A classic decision which helps resolve classification disputes is found in the decision of the Supreme Court, in the case of *Union of India v. Delhi Cloth and General Mills* [AIR (1963) SC 791]. Although, the case relates to classification of goods, for excise duty purposes it has great significance to the subject matter of discussion as it lays down the philosophy underlying classification of goods. In that case, the respondents were manufacturers of vegetable products known as vanaspati. In the course of manufacture of this product, they were purchasing from the open market groundnut and til oil and subjecting them to different processes before applying the process of hydrogenation which was essential for making vanaspati. The excise authorities wanted to tax this oil at this intermediary stage, under tariff item 23 of the Central Excise Tariff (as it then was) as "refined oil, "all sorts, in or in relation to the manufacture of which any process is ordinarily carried on with the aid of power". The Supreme Court held that excise duty being a tax on manufactured goods and not on their sale, the respondents would no doubt be liable to duty if they produced "refined oil" as "known in the market" at an intermediary stage and since there could be no refined oil as known in the market without the process of deodrisation, they could not be said to have produced "refined oil" as sought by the taxing authorities.

In *South Bihar Sugar Mills v. Union of India* [AIR (1968) SC 922] again, another case of excise classification further illustrates the point. There, the appellants were manufacturing sugar by carbonation process and paid duty on sugar under the relevant tariff item (item No. 1 of the Central Excise Tariff as it then was. For the purpose of this carbonation process, the mills had produced a gas known as "Kiln gas" which besides containing carbon dioxide, also contained other impurities like nitrogen, oxygen and a small quantity of carbon monoxide. According to the excise authorities this "kiln gas" attracted duty under the relevant tariff items (item No. 14(iv) of the Central Excise Tariff as it then was, relating to "compressed liquified or solidified gases including carbonic acid (carbon dioxide). The manufacturers on the other hand disputed this claim on the ground that what they generated was not carbon dioxide as was known to the market and that it was impure gas, containing, besides carbon dioxide certain other impurities too, which was not the case with carbon dioxide available in the market.

Applying the ratio of its earlier decision in the DCM'S case above referred to, the Supreme Court held that the "mixture of gases produced from the Kiln" was known both in the trade and Science as 'Kiln gas' and not as carbon dioxide and hence not liable to duty as contended by the excise authorities.

The Supreme Court observed that the Act, charged duty on manufacture of goods. The word "Manufacture" implies a change but every change in the raw material is not "manufacture". There must be such a transformation that a "new and different" article must emerge having a distinctive name, character and use. The Court observed:

"The duty is levied on goods. As the Act does not define goods, the legislature must be deemed to have used that word in its ordinary dictionary meaning. The dictionary meaning is that to become goods, it must be something which is known to the market".

In *Ramavtar Budripasad v. Assistant Sales Tax Officer* [AIR (1961) SC 1325], the question before the Supreme Court was whether "betal leaves" could fall within the category of "vegetables" for purposes of assessment to sales tax and the court held that the latter could not include within its scope the former, since both were two distinct and separate commodities. The Court held that since the said expressions were not defined by the statute (C.P. and Berar Sales Tax Act 1947 as amended by the C.P. and Berar Act of 1948), and being a word of "every day" use, it must be construed in its proper sense, meaning "that sense in which people conversant with the subject matter with which the statute is dealing would attribute to it.

In *Commissioner of Sales Tax, Madhya Pradesh v. Jaswant Singh*, the Supreme Court further explained the basis for classification of goods. The question before the Court was whether "charcoal" was included in "coal" for assessment of sales tax. It was held that the Sales Tax Act being one levying a tax on goods must, in the absence of a technical term or a term of science or art, be presumed "to have used an ordinary term as coal according to the meaning ascribed to it in "common parlance". Viewed from this point, the Court held that both a merchant dealing in coal and a consumer wanting to purchase it would regard coal not in its geological sense but in the sense as "ordinarily understood" and would therefore include charcoal in the term "coal".

In *Annapurna Carbon Industries v. State of Andhra Pradesh* [AIR (1975) SC 1418] the Supreme Court laid down the test of "predominant" or "ordinary purpose" as deciding factors for determination of classification of goods. It was not the exceptional use or extraordinary use to which the goods could be put to but how predominantly it was used. The Supreme Court further laid down that the fact that the article could be put to any other use also would not detract from the position explained and that the test of general or predominant user was the true test in such matters.

From the above discussion it is clear that while classifying goods for duty purposes due regard should be

had to the above principles and it is open for the importer to help the correct classification by establishing how the commodity was popularly known in the particular trade or business in connection with which the goods imported would be used.

In *Commissioner of Sales Tax Madhya Pradesh v. Bhaket Rai* (19 Sales Tax Cases, 285) the Madhya Pradesh High Court, considered the question whether coconuts, groundnut kernel and jira were oil seeds attracting duty under the relevant tariff item (Item 3 of Part II of Schedule I) of the Madhya Pradesh General Sales Tax Act, 1958. The Sales Tax Tribunal had taken the view that these articles were oil seeds in as much as they were seeds and oil could be extracted from them. On reference the High Court took the view that the term oil "seeds" not having been defined by the statute, should be construed in that sense which "people conversant with the subject matter with which the statute was dealing would attribute to it." Those articles, in the opinion of the Court, were not known as "oil seeds" in common parlance used principally for the extraction of oil and therefore, could not attract the tax.

The Punjab High Court in *Kanpur Textile Finishing Mills* case [AIR (1956) Punjab 130] laid down that:

When dealing with a particular business or transaction words are presumed to have been used with the particular meaning with which they are used and understood in the particular business."

In *National Hurricane Works v. Union of India* [AIR (1967) Delhi 156], the Delhi High Court dealing with the Import Tariff laid down that if a particular term or word has not been defined in the tariff, then one has to go by the ordinary meaning of the term and that if an item falls specifically under one entry, it cannot by the "process of stretching be brought to fall under another entry".

It is a settled legal position that if words or expressions used in the tariff are not defined in the body of the statute or the tariff then, regard shall be had to technical opinions, dictionaries and treatises on the subject, including ISI standards.

The basic principle underlying adjudication is to act judicially and not arbitrarily.

The Supreme Court has categorically laid down in *G. Nageshwara v. A.P.S.R.T. Corporation* (AIR) (1959) SC 308, that rules of natural justice require that quasi judicial authorities empowered to decide any dispute must decide the cases without any bias on the principle that "justice should not only be done, but also should manifestly and undoubtedly be seen to be done."

In *Shri Baidyanath Ayurvad Bhawan Ltd. v. Asstt. Collector of Central Excise*, Allahabad, the Allahabad High Court was perturbed that even though the collector (appeals) had directed de-novo adjudication of the case, a personal hearing was not granted by the Adjudicating authority (even though a specific request in this behalf had been made by the petitioner) on the ground that the Petitioner had filed some papers on the date of hearing which could not take place on account of pre-occupation of the authorities. The Court held that filing of papers cannot be equated with personal hearing, and on this count alone, the order of the adjudicating authority passed on de-novo consideration of the matter was liable to be quashed.[1986(25) ELT-II(ALL)].

In *Banwarilal Roy's* case [AIR (1948) Calcutta 776] the Calcutta High Court laid down that: "a judicial or quasi-judicial act on the other hand implies more than mere application of the mind or the formation of the opinion. It is a reference to the mode or manner in which that opinion is formed. It implies a 'proposal', an 'opposition' and the 'decision' on the issue."

In *Soorajmal v. Assistant Collector of Customs* [AIR (1952) Calcutta 103] the Calcutta High Court laid down that:

"It is the duty of the customs authorities to 'adjudge' (i.e. decree judicially) the penalty. In other words, to act judicially or quasi-judicially. The fundamental rules of judicial procedure or the principles of natural justice require that a proper hearing and opportunity be given to the person before the rights of such a person are affected by any decision or adjudication. Where the customs authorities impose extra duty, acting in a high handed and an arbitrary manner, arrive at their decisions on extraneous and irrelevant considerations without giving proper opportunity to the petitioner to put his case before the customs authorities and later on demand the extra duty, there has been a denial of natural justice and violation of the fundamental principles of judicial procedure and a writ of certiorari does lie even though there may be an alternative remedy open to the petitioner by way of an appeal".

The Calcutta High Court while observing as above relied on the Supreme Court decision in *Province of Bombay v. Khushaldas Advani* [AIR (1950) S.C. 222] and came to the aforesaid conclusion.

Classification of goods is an intricate but well defined exercise. Reading and interpreting a tariff entry cannot be done in any casual or non-challant manner. Words and expressions found in a tariff have to be properly understood and harmonized. They cannot be taken out and read in *vaccum*, so to say, nor can entries be read, out of context.

In *Ex-QUIZ TI v. State of Tamil Nadu* [1986 (25) ELT 6 (MAD)] the Madras High Court observed: "....the Supreme Court held that in determining connotation of words and expressions describing an article or commodity.... which is taxed..... if there is one principle fairly well settled, it is that the words or expressions must be construed in the sense in which they are understood in that trade by the dealer and the consumer and that it is they who are concerned with it, and it is the sense in which they understand it that constitutes the definite index of the legislative intention when the statute was enacted".

In *Madanvathi's case* [AIR (1960) Mysore 299, 301] the Mysore High Court (as it then was) pointed out that:

"the first and foremost rule of interpretation is the rule of grammatical interpretation,, the legislature must be deemed to have intended what it has said. It is no part of the duty of the court to presume that the legislature meant something other than what it said. If the words of the section are plain and unambiguous then there is no question of interpretation or construction. The duty of the Court is to implement these provisions".

In *Indye Chemicals v. Collector of Central Excise Ahmedabad* -1986 (25) ELT 318 (Tribunal), it has been reiterated that Exemption notifications are to be construed strictly and in accordance with the plain meaning of the words used therein and if there is any doubt, the benefit of that doubt should go to the assessee so that the tax burden is reduced.

In *Goolabchand's case* [AIR (1951) MB 11 (FB)] it has been laid down that:

"If a plain word carried a plain sense in the English language, however strict the law may interpret it, it will not ignore the ordinary meaning which it carries".

Crawford an authority on statutory construction has stated that:

"Where a word used by the legislature has fixed technical meaning; it is to be taken in that sense. The technical words and phrases of the law are presumed to have been used in their proper technical signification when used in statutes....."

Maxwel in his interpretation of statutes has stated that:

"the first and foremost elementary principle is that it is to be assumed that the words and phrases of technical legislation are used in their technical meaning if they have acquired one otherwise in their ordinary meaning".

In *United States v. Brown* [333 US (8)], it has been laid down : “no rule of construction necessitates acceptance of an interpretation of a statute resulting in absurd consequences”.

In *Robertson v. Day* (5AC 62, 69) the privy Council has said:

“It is a legitimate rule of construction to construe words.....with reference to the words found in immediate connection with them”.

In *Commissioner of Income Tax, Bombay v. Reid* (AIR (1931) Bombay 333 it has been laid down that:

“In construing a taxing Act, the Court is not justified in straining the language in order to hold a subject liable to tax”.

The Supreme Court in *Sales Tax Commissioner v. Modi Sugar Mills* [AIR (1901) SC 4047] laid down that:

“In interpreting a taxing statute equitable considerations are entirely out of place. Nor can taxing statutes be interpreted on any presumptions or assumptions. The Court must look squarely at the words of the statute and interpret them. It must interpret a taxing statute in the light of what is clearly expressed, it cannot imply anything which is not expressed; it cannot import provisions in the statute so as to supply any assumed deficiencies.”

The CEGAT, in *Venus Engineering Pvt. Ltd. v. Collector of Central Excise, Baroda* [1986 (25) ELT 553 (TRIBUNAL)] observed that it is hazardous to interpret a word in accordance with its definition in another statute or statutory instrument, more so when these are not dealing with any cognate subject. The subject of the Factories Act is far from being cognate with the subject of the Central Excise Act - one deals with taxes and the other with places where goods are manufactured. In the circumstances, the word “worker” in the Central Excise Act must be given the same meaning which it receives in ordinary parlance or is understood in the sense in which people conversant with the subject matter understand it and not that attributable to it under the Factory Act.

In the matter of availment of exemptions, it has been laid down by the Kerala High Court in the case of *Rice and Oil Mills* [1981 ELT (KER) 59] that denial of an exemption notification would tantamount to violation of fundamental right. It is also a settled legal position that in the matter of exemption notifications, the authorities cannot abridge, alter, amend or nullify the scope of a valid notification. Benefits flowing out of a valid notification cannot also be denied. An importer who does not have sufficient finances to clear the goods or if he does not require all the goods imported for consumption at one time, may file a Bill of Entry for warehousing under the warehousing provisions, so that appropriate duty may be paid at the time of actual clearance of the goods from the warehouse.

(b) Customs Act and Exemption Notifications

It has already been seen that under the Customs Act (Section 25 of the Act) power has been conferred on the Central Government to exempt certain goods from the levy of customs duty. An importer has to necessarily keep a proper track of exemption notifications. The exemptions notifications may either be without any reference to any given time period or may be with reference to a particular period. In the former case, the exemption notification can be withdrawn at any time by Central Government. It is therefore necessary to envisage this eventually while negotiating contracts for sale of goods after their import into India, because Customs Duty liability will increase the cost of import which should normally be reflected in selling price. Even if the imported goods are not to be sold but are to be captively consumed, the levy of import duty by withdrawing the exemption granted earlier would have the effect of increasing the cost of production. If the imported goods are Plant and Machinery even then its effect would be to increase the cost of project. Even in a case where exemption has been given for a given period of time, the Central Government may withdraw the exemption notification before the expiry of the given period of time. To take

an example, an exemption notification issued on 1.10.96 effective up to 1.10.99, may be withdrawn by the Government before 1.10.99, with the result an importer who placed an order for import of goods in the hope that they are exempted from duty may be faced with the shocking problem to pay the duty because the exemption notification has been withdrawn before 1.10.99. Now the question is, whether such a withdrawal of exemption before the expiry of normal period up to which it must have run can be challenged on the ground of promissory estoppel. The Judicial view seems to be that promissory estoppel cannot be pleaded against the Government, because withdrawal of the exemption notification under Section 25 is in public interest and such a withdrawal is a legislative function. These aspects must be borne in mind whenever any goods are imported on the basis of an exemption notification.

(c) Customs Act and CENVAT

Yet another aspect of interest in customs law is that the countervailing duties payable on the import of certain goods have to be properly accounted for in the documents. Suitable endorsement of the intention to avail CENVAT credit must be made on the Bill of entry. This is because the same Bill of entry may not be used for claiming any duty drawback on exports. This is because CENVAT credit can be availed in respect of countervailing duties also. If the importer is a canalising Agency and the goods are supplied by the canalising Agency to the Manufacturer, such a manufacturer must impress upon the canalising agency for issue of a certificate in respect of countervailing duties paid on the goods. Only on the basis of such a certificate the manufacturer would be able to get CENVAT credit.

(d) Customs Act and Duty drawback

As regards exports are concerned a matter of subtle importance is the claims for duty drawback on the export of goods. The interesting question that has been agitated more than once before various judicial forums is, when does export takes place, whether on the export goods passing into the control of Customs Department or when the export goods reach the buyer located beyond the territorial waters of India. Judicial decision on this point are quite encouraging. The view is that once the export goods pass into the control of the Customs Department so as to be out of the control of the exporter any longer, the export is supposed to be complete. This issue is very important because there may be two eventualities.

After the export goods passes into the control of Customs Department and the goods have been boarded on the ship or have been kept for boarding on the ship, there may be a loss or destruction due to fire or action of the sea or due to any other cause. Secondly, though the goods are safely boarded on the ship, but before they cross the territorial waters of India, there may be loss or damage to the goods on board or the whole ship may be lost. In such situations, it is proper to cite judicial rulings wherein some of the High Courts declared that export is complete when the export goods pass to the customs control notwithstanding the fact that thereafter they get lost or destroyed before crossing the territorial waters of India.

(e) Customs Act and Record Keeping

Last but not the least is the proper documentation and record keeping. The maintenance of correct and proper records would avoid any penal action being taken by the excise department for non-compliance with any particular rule or notification. In this context, it is necessary to be conversant with various regulations rules and the forms prescribed under the customs laws. These have been adequately explained in the preceding study lessons. A tax planner would therefore labour to keep track of various amendments brought about to various rules forms etc. so that the records and registers are at all times in consonance with the statutory requirements.

EXCISE LAW AND TAX PLANNING

A proper tax planning exercise has to be done so as to ensure due compliance with the statutory provisions

and also to reduce the incidence of duty to the minimum. In fact a proper tax planning exercise in Central Excise Law demands:

- (i) An in-depth knowledge of substantial provisions;
- (ii) A thorough knowledge of procedural formalities;
- (iii) A continuous follow-up of various Exemptions Notifications;
- (iv) Awareness to various Court Rulings; and
- (v) Ability to reason out and argue one's point of view.

At the outset it is a wiser part of discretion to avoid basing tax planning on very tenuous reasoning and controversial interpretations. At the same time when the rulings of the Courts carry considerable conviction it would not be advisable to ignore them. Wherever the planning is done on premises which may not find a favour with the Courts or the legislature ultimately, it is desirable to make suitable provisions in the accounts to meet the duty liability that may arise in future for past transactions. Alternatively, while entering into contract of sale of goods, a manufacturer may do well to provide in the contract note that, should additional demand of duty be made by the Government on him, the same would be recovered from the purchaser (this is however subject to the advisability of including such term from a purely commercially strategic point of view).

Some broad areas of tax planning with reference to Central Excise Laws are discussed herein below:

(a) Classification of goods

Indirect taxes are levied on goods either at ad valorem or at specific rate or a combination of the two. Irrespective of the type of duty, the rate and the amount of duty would in almost all cases inter alia depend on classification of the goods. As wrong classification of goods would lead to many complications, it is better to get the classification of goods decided by the department.

(b) Valuation

Valuation of excisable goods is a very important aspect of Central Excise Law. As many of the excisable goods attract ad valorem rates of duty, a manufacturer should be quite conversant with the relevant provisions in this regard under the Central Excise Act and the Rules. As on 1.7.2000, the new Section 4 substituted by the Finance Act, 2000 read with Valuation Rules, 2000 framed thereunder apply to such cases. In nutshell, the new provisions seek to tax the goods based on "transaction value" and barring the substitution of the basis of value from "normal price" to "transaction value" and some alteration in the definition of the terms "related person" and "place of removal", the provisions of valuation under the new law substantially remain the same. Suffice here to say that the manufacturer should try to meticulously plan the pricing of its products, as the prescription under the new law is that, so long as the price is the sole consideration and the buyer is not related to the assessee, then on each removal the value should be the "transaction value". Meaning thereby as long as transaction is not tainted by either the relationship or any additional consideration whatever price is charged by the assessee is bound to be accepted by the Revenue. Since "transaction value", which is going to be the basis for determination of value in majority of the cases, refers to "price actually paid or payable", the whole lot of problems related to adjustment of the sale price for various abatements like discount, cost of packing, etc. required to be applied under the erstwhile law for arriving at the assessable value which gave rise to needless litigation at times, would become redundant.

Wherever transaction value is not applicable, i.e. as provided under clause (b) of Section 4(1) which says that in any other case, including case where the goods are not sold, the value is to be determined in terms of

rules framed for this purpose, which are called “Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 where (i) time of delivery is different from the time of removal; or (ii) place of delivery is different from the place of removal; or (iii) buyer is a related person; or (iv) there is additional consideration flowing from the buyer to seller. The cases of removal which does not amount to sale could be stock transfers to depots or other units of the assessee, or captive consumption of excisable goods. Under these circumstances, the value has to be determined in terms of rules framed for the purpose.

A few aspects on abatements/additions under the new provisions as compared to the old provisions, to be kept in mind are:

1. Discount

Under the old Section 4(4)(d)(ii), all discounts allowed at the time of removal in accordance with normal trade practices were permitted to be deducted from the wholesale price. Under the substituted new law, the definition of transaction value refers to “price actually paid or payable”, and thus, can be construed to mean that price actually paid is net of discount and hence, discount does not form a part of the price at all. The Board (Central Board of Excise and Customs) has, in its clarificatory circular, dated 30.6.2000 at para 9 states that “no reference to discount is necessary in new Section 4 as the duty is chargeable on the net price paid or payable”. Thus, if in any transaction a discount is allowed on declared price of any goods and actually passed on to the buyer of the goods as per common practice, the question of including the amount of discount in the transaction value does not arise. Discount of any type of description given on any normal price payable for any transaction will therefore, not form part of the transaction value of goods, e.g. quantity discount for goods purchased, cash discount for prompt payment, etc.”.

2. Packing cost

Packing charges do not find a place in the scheme of the new valuation code, the distinction between disposable and durable/returnable packing, primary, packing, secondary packing, special secondary packing introduced by the Courts cases their relevance. Generally, under all statutes, which seek to tax commodities, packing cost has always been held includable in the assessable value. Para 12 of the Board circular, dated 30.6.2000 ibid states that all packing costs would be includable in the value.

3. Cost of after sale service, etc.

Special care may have to be taken under the new provisions in regard to certain ‘post manufacturing expenses’ with reference to inclusions or non-inclusions of such expenses earlier done based on the judgements in the cases of “Bombay Tyre International and MRF Ltd.”. As per the definition of “transaction value” under the new law, use of the words “any amount” “in connection with..... any other matter” and “servicing” would bring within its scope many expenses which were hitherto considered excludable being post removal expenses. The definition not only includes actual payment but also any provision made for such expenses about which also one has to be very careful.

(c) Excise concessions on export of excisable goods

Exporters of excisable goods are entitled to several benefits. Under the schemes available in the Excise Law, the exporter of excisable goods can avail following facilities:

- To export excisable goods on payment of excise duty and to claim refund of such duties subsequent to the export.
- To export the goods without paying excise duty but on the basis of a bond being executed to fulfill the obligation to export.

- (c) To claim rebate of duty paid on excisable goods used as inputs in the manufacture of goods which are exported.
- (d) To process excisable goods required as inputs for manufacture of goods to be exported, without paying duty on such inputs.

Besides, the CENVAT Scheme also contains in-built provisions to act as a major incentive for production for export, which the exporter can make use of.

(d) Refund claims

The assessee should ensure that all refund claims are prepared in time so that the right to claim is not lost. Refund can be claimed within one year of the relevant date subject to the provisions of Section 11B of the Central Excise Act. Where an order of the Assistant Commissioner of Central Excise classifying the product under a particular tariff item, though appealable, is not challenged by the assessee, then the classification order is not liable to be questioned, and the matter is not to be reopened in a proceeding for refund, which is in the nature of execution of a decree/order. That is how the relevant question arising for answer in the appeal before the Supreme Court in *Collector of Central Excise, Kanpur v. Flock (India) Pvt. Ltd.* (Civil Appeal No. 2552 of 1989, decided on August 4, 2000) was answered by a Division Bench of the Supreme Court comprising Mr. Justice B.N. Kirpal and Mr. Justice D.P. Mohapatra. So one has to be careful that excise classification by Assistant Commissioner becomes final if not appealed against and cannot be challenged in proceedings for refund.

(e) CENVAT

CENVAT Scheme (which replaced erstwhile MODVAT Scheme) offers considerable scope of planning. A manufacturer intending to avail CENVAT may look for his requirements of various spares and components etc. in the small scale industry sector. This is because small scale units enjoy the benefit of exemptions from central excise duty/levy of duty at concessional rates. Where the items produced by the SSI unit happens to be duty exempt whereas the raw material is duty paid, and benefit of CENVAT credit of duty paid on the raw material can not be availed by the SSI unit. The manufacturer can procure the material himself and send the same to SSI unit for job work and avail the benefit of CENVAT credit of duty paid on the raw material. But in order to be able to avail these benefits it is essential for the manufacturer to ensure that the small scale unit from whom supplies are being obtained is one availing exemption from duty on the basis of the value of its clearances pursuant to a notification issued in this behalf.

It is equally essential for the manufacturer of final products to ensure that a small scale unit supplying parts and components pays duty at a concessional rate. In other words, where goods are obtained from small scale industrial units working under the applicable notification paying nil rate of duty (on its clearances up to exemption limit) the purchaser (finished goods manufacturer) would not be entitled to any credit under CENVAT. It therefore may become necessary for the finished goods manufacturer to impress on the small scale units not to avail any exemption from duty for clearances upto the exemption limit. The small scale unit would be only more willing not to avail duty exemption benefit if a purchaser makes a firm commitment to place the orders. The small scale unit can always opt for paying duty if its own eligible inputs are dutiable and attract higher rate of duty than that payable on its finished products.

While working under the CENVAT rules, a manufacturer should ensure meticulous adherence to rules in regard to sending of goods for doing any job work or while sending the raw materials for manufacture of intermediate products under various notifications or while dealing with wastes.

(f) Small Scale Units

Sometimes manufacturers of reputed goods enter into agreements with other manufacturers, may be in the Small Scale Sector by which they undertake to supply drawings, designs under the specifications to ensure quality. To take a practical example, a manufacturer of reputed brand of electrical fans may supply essential specifications, designs and drawings relating to the manufacture and the manufacturer would adhere to the specifications and produce the electrical fans. The supplier of the drawings and designs may examine the quality and then buy the goods (fans) from the small scale manufacturer. In such cases the question that has been agitated before the courts has been that the supplier of drawing designs is the manufacturer and not the small scale unit which actually manufactures the goods (fans). The attempt of the revenue at times has been to include in the selling price of the small scale industrial unit of the goods manufactured by it, the value of the trade mark of the supplier of the designs and drawings. Trade mark may be either affixed by the small scale unit itself or by the supplier. Supplier of drawings and designs cannot be regarded as manufacturer because under the excise law only a person who is actually manufacturing the excisable goods can be regarded as manufacturer provided such a manufacturer is not a dummy. And once the manufacture has been done by the SSI unit and it sells the goods on a principal to principal basis, for a purely commercial consideration, to the supplier of drawings and designs, there cannot be any further addition to the value of the excisable goods, attributable to the Trade Mark of the supplier of drawings and designs. Reference may be made on these points to following case laws—*Union of India and Others v. Cibatual Ltd.* 1985 22 ELT 302 (SC); *Joint Secretary of Government of India v. Food Specialities Ltd.* 1985 22 ELT 324 (SC); *Collector of Central Excise v. Modo Plant (P) Ltd.* 1985 21 ELT 187 (CEGAT); *Jay Engg. Works Ltd. v. Collector of Central Excise* 1985 21 ELT 299 (CEGAT); *Lucas Indian Service Ltd. v. Collector of Central Excise* 1984 16 ELT 415 (CEGAT).

With the result the Small Scale Unit may either pay no duty (if covered under the relevant applicable notification) up to the exemption limit or may pay concessional rates of duty. In either event there is double benefit. One, a lower assessable value due to a lower selling price which in return is a result of lesser cost of production, and other, a lower duty incidence in view of special benefits extended to small scale units. The manufacturers in the large scale sectors may profitably exploit such methods of decentralising production. There is however a note of caution that such decentralised production centres should not be mere dummies.

LESSON ROUND UP

- In common language, “Promissory” means “related to a promise”, and “estoppel” is a legal term that essentially means an enforced bar or ban. Judges use the doctrine to ban one person from going back on promise.
- The Doctrine of Promissory Estoppel marches with hypothesis that a promise given by the State is binding on the Government in the prescribed circumstances.
- The Doctrine of Estoppel can be revoked by the government if it is in the public interest and it cannot be enforced when it is prohibited by law.
- Tax can be planned in the Excise and Custom in the certain provisions such as : classification of goods, Exemption Notification by proper utilization of Cenvat Credit, duty-drawback, valuation of goods, export concessions, etc.

SELF-TEST QUESTIONS

1. What is the relevance of 'Doctrine of Promissory Estoppel' in the fiscal laws?
 2. What are the relevant areas in which tax planning could be done with regard to levy of duties of Customs?
 3. What is the scope of tax planning with regard to levies of the Central Excise?

SUGGESTED READINGS

- (1) Central Excise Manual — *Taxmann*
 - (2) Customs Law Manual — *Taxmann*
 - (3) Excise Law Times — *Centax Publications, New Delhi*

Lesson 9

Service Tax: Introduction and Administration

LESSON OUTLINE

- Background
- Constitutional validity
- Administrative mechanism
- Limbs of service tax laws
- Taxability of services
 - Meaning of service
 - Declared services
 - Negative list of services
 - List of exemptions under mega notification
 - Place of provision of services rules
- Computation of service tax
- Lesson round up
- Self Test Questions

LEARNING OBJECTIVES

The Service tax was introduced on the recommendation of Dr. Raja Chelliah Committee on tax reforms. Initially it was imposed at a uniform rate of 5% in the Union Budget for 1994-95 on 3 services. In a journey of about 19 years, it has seen various changes. Finance Act, 2012 has made remarkable changes in service tax legislation whereby the concept of Positive list of Taxable services has been replaced with a negative list. There is paradigm shift in the way services are taxed. Now all services except as notified in Negative list or exemption list are subject to applicability of service tax.

At the end of this lesson, you will learn

- The principles underlying the introduction of service tax
- Constitutional background of service tax
- Administrative machinery of service tax
- Components which provides for governance of service tax law
- Place of Provision of Services Rules
- Applicable rate of service tax.

Service tax is administered by the Central Board of Excise and Customs (CBEC) which is under the control of the Department of Revenue, Ministry of Finance. CBEC administers the service tax through the Central Excise Department. A separate cell called the service tax cell, under each Commissionrates of central excise has been created for the purpose. Considering large number of assessees, CBEC has also established Service Tax Commissionrates in some cities

BACKGROUND

As the economy grows and develops, the contribution of the services sector becomes more substantial. Hence, tax on services becomes substantial revenue for the Government. Although Service tax is a concept of the modern era where developed economies as well as developing economies find over 70% of their gross economic output coming from the service sector. Service tax was there in vogue even in the Mauryan period in India. Ms. Romila Thapar in her "Asoka and the Decline of the Mauryas", at page 72 (London 196, paperback edition, 1997, by Oxford) points out that services of weapon and implement makers were required to be provided to the state for a certain number of days in a year. This was a form of service tax in that period. But in the modern context, because of the increasing contribution of the service sector to the GDP of an economy, the importance of service tax is growing. As under the WTO agreements governments are required to reduce customs tariffs, governments are considering increase in service taxes revenues as a compensatory revenue generation mechanism. In terms of economics, tax on services is an indirect tax. This is because the burden of service tax can be passed on to the customer i.e., the recipient of the service. The service provider may also bear the burden of the tax by not passing or charging the same to a customer.

Example: How the burden of service tax shifted on the consumer?

Mr. Mohit is practicing Company Secretary, he represent before the Tax Authorities on behalf of Mr. Neeraj and raise a invoice of ₹1,00,000 plus service tax @12.36%.

Here, Mr. Neeraj is the client and he is required to pay the service tax of ₹12,360 in addition to the value of services. Subsequently Mr. Mohit deposit the sum to treasury of Central Government.

The ultimate outcome of this is that the burden of service tax is on the consumer.

The Tax Reforms Committee headed by Dr. Raja J Chelliah recognized the revenue potential of the service sector and recommended imposition of service tax on selected services (selective approach or positive list approach). Consequently the service tax was imposed at a uniform rate of 5% in the Union Budget for 1994-95 on 3 services.

Finance Act, 2012 has made remarkable changes in service tax legislation whereby the concept of Positive list of Taxable services has been replaced with a negative list. A negative list of services implies that there is, a list of services which are not be subject to service tax. Service tax will not be chargeable on the services mentioned in the negative list and which are exempted by issue of notification. This is in contrast to the earlier method of taxation of services where the law had provided definition for each taxable service and all other undefined services were outside the preview of Service Tax.

Reason for Imposition of Service Tax:

In *ALL INDIA FEDN. OF TAX PRACTITIONERS v. UNION OF INDIA* 2007 (7) S.T.R. 625 (S.C.) the Hon'ble Supreme Court of India has mentioned the following reasons for the imposition of service tax.

Service tax is an indirect tax levied on certain services provided by certain categories of persons including companies, association, firms, body of individuals etc. Service sector contributes about 64% to the GDP. Services" constitute heterogeneous spectrum of economic activities. Today services cover wide range of activities such as management, banking, insurance, hospitality, consultancy, communication, administration, entertainment, research and development activities forming part of retailing sector. Service sector is today occupying the centre stage of the Indian economy. It has become an Industry by itself. In the contemporary

world, development of service sector has become synonymous with the advancement of the economy. Economics hold the view that there is no distinction between the consumption of goods and consumption of services as both satisfy the human needs.

In late seventies, Government of India initiated an exercise to explore alternative revenue sources due to resource constraints. The primary sources of revenue are direct and indirect taxes. Central excise duty is a tax on the goods produced in India whereas customs duty is the tax on imports. The word "goods" has to be understood in contradistinction to the word "services". Customs and excise duty constitute two major sources of indirect taxes in India. Both are consumption specific in the sense that they do not constitute a charge on the business but on the client. However, by 1994, Government of India found revenue receipts from customs and excise on the decline due to W.T.O. commitments and due to rationalization of duties on commodities. Therefore, in the year 1994-95, the then Union Finance Minister introduced the new concept of "service tax" by imposing tax on services of telephones, non-life insurance and stock-brokers. That list has increased since then. Knowledge economy has made "services" an important revenue-earner.

At this stage, we may refer to the concept of "Value Added Tax" (VAT), which is a general tax that applies, in principle, to all commercial activities involving production of goods and provision of services. VAT is a consumption tax as it is borne by the consumer.

In the light of what is stated above, it is clear that Service Tax is a VAT which in turn is destination based consumption tax in the sense that it is on commercial activities and is not a charge on the business but on the consumer and it would, logically, be leviable only on services provided within the country. Service tax is a value added tax.

As stated above, service tax is VAT. Just as excise duty is a tax on value addition on goods, service tax is on value addition by rendition of services. Therefore, for our understanding, broadly "services" fall into two categories, namely, property based services and performance based services. Property based services cover service providers such as architects, interior designers, real estate agents, construction services, mandap Keepar etc.. Performance based services are services provided by service providers like stock-brokers, practicing company secretaries, practising chartered accountants, practising cost accountants, security agencies, tour operators, event managers, travel agents etc..

Government of India in order to tap new areas of taxation and to identify the hidden one appointed Tax Reforms Committee under the Chairmanship of Dr.Raja J Chelliah in August, 1991. The recommendations made by the Committee were accepted and the Service Tax was introduced in the Budget for 1994-95 through the Finance Act, 1994. Under the said enactment, Service Tax is the tax on notified services provided or to be provided. After its introduction, the constitutional validity of the services taxed by the Central Government was challenged before the Constitution Bench of this Court which took the view that the Central Government derived its authority from Entry 97 of List I of the Seventh Schedule to the Constitution for levying tax on services provided.

CONSTITUTIONAL VALIDITY

As per Article 246 of the Constitution of India, law can be enacted by Parliament or the State legislature, if such power is given by the Constitution of India.

Article 265 of the Constitution lays down that no tax shall be levied or collected except by the authority of law.

Schedule VII divides this subject into three categories –

- (a) Union list (only Central Government has power of legislation)
- (b) State list (only State Government has power of legislation)
- (c) Concurrent list (both Central and State Government can pass legislation).

Entry 97 of the Union list is the residuary entry and empowers the Central Government to levy tax on any matter not enumerated in state list or the concurrent list.

In 1994, the service tax was levied by the central government under the power granted by the entry 97 of the union list.

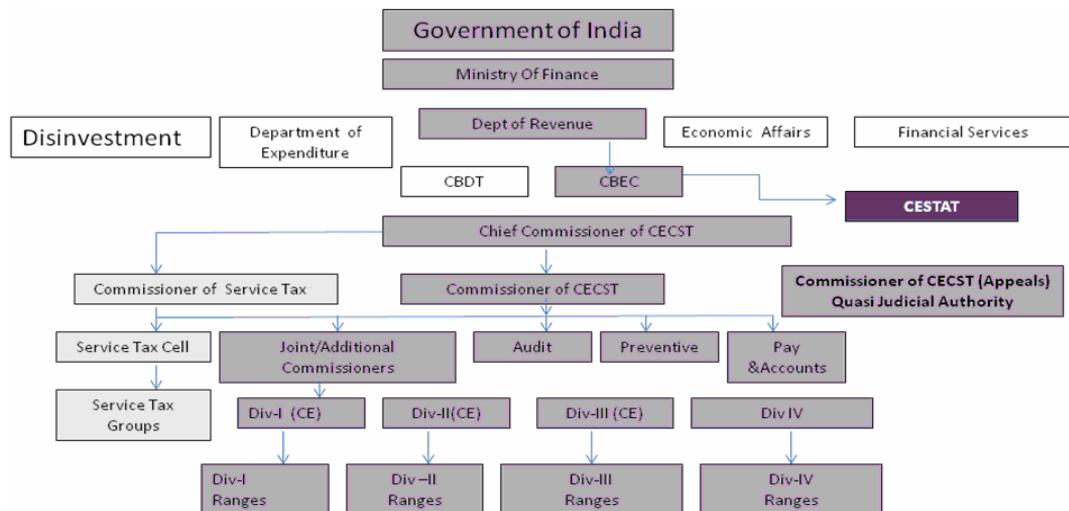
Thereafter in 2003 the government has passed the constitution (88th Amendment Act, 2003) which provides for the levy of service tax by the centre through the insertion of article 268A to the constitution. In addition to article 268A, entry 92C has been inserted in the union list to make the enactment relating to service tax a subject matter of union list.

Students may note that entry No.92C has not yet been made effective by the parliament and service tax is still governed by the entry 97 of the union list.

ADMINISTRATIVE MECHANISM

Service tax is administered by the Central Board of Excise and Customs (CBEC) which is under the control of the Department of Revenue, Ministry of Finance. CBEC administers the service tax through the Central Excise Department. A Central Excise Commissionate establishes a separate cell called the service tax cell for the purpose of administration of Service Tax within its jurisdiction. Considering large number of assessees, CBEC has also established Service Tax Commissionerates in some cities. There are six Commissionerates located at metropolitan cities of Delhi, Mumbai, Kolkata, Chennai, Ahmadabad and Bangalore which deal exclusively with work related to Service Tax. These Commissionerates are supervised by the jurisdictional Chief Commissionerate of Central Excise.

Administrative Structure – Service Tax



Division in charge : Assistant / Deputy Commissioner Range in Charge: Superintendent

NOTES:

CESTAT	= Custom Excise Service Tax Appellate Tribunal
CECST	= Central Excise, Customs & Service Tax
Div	= Division

When separate Service Tax Commissioner is Constituted, then Commissioner of CECST, Commissioner of CEC, Service Tax Cell Comes under Service Tax Commissioner.

When separate Service Tax Commissioner is not Constituted, then Service Tax Cell Comes under Commissioner of CECST.

The above Chart is illustrative, as under the Commissioner of CECST or Commissioner of CEC there are other functional departments like Adjudication, Refunds, Technical Cell, Laboratory, Establishment.

TAXABILITY OF SERVICES

Service Tax is levied vide Finance Act, 1994 (the Act). The Finance Act, 1994 applies all over India except the state of Jammu & Kashmir.

With effect from 1st July 2012, a new charging Section 66B has been inserted by the Finance Act 2012. Section 66B provides that there shall be levied a tax (hereinafter referred to as the service tax) at the rate of twelve per cent on the value of all services, other than those services specified in the negative list, provided or agreed to be provided in the taxable territory by one person to another and collected in such manner as may be prescribed.

The taxation of services is completely overhauled from positive approach or selective services to negative list approach. Now, no classification of services is required for the purpose of taxability. Moreover, only services rendered in taxable territory are taxable for which Place of Provision of Service Rules, 2012 ('PPSR') are prescribed and with this Import of Services and Export of Services Rules has been rescinded.

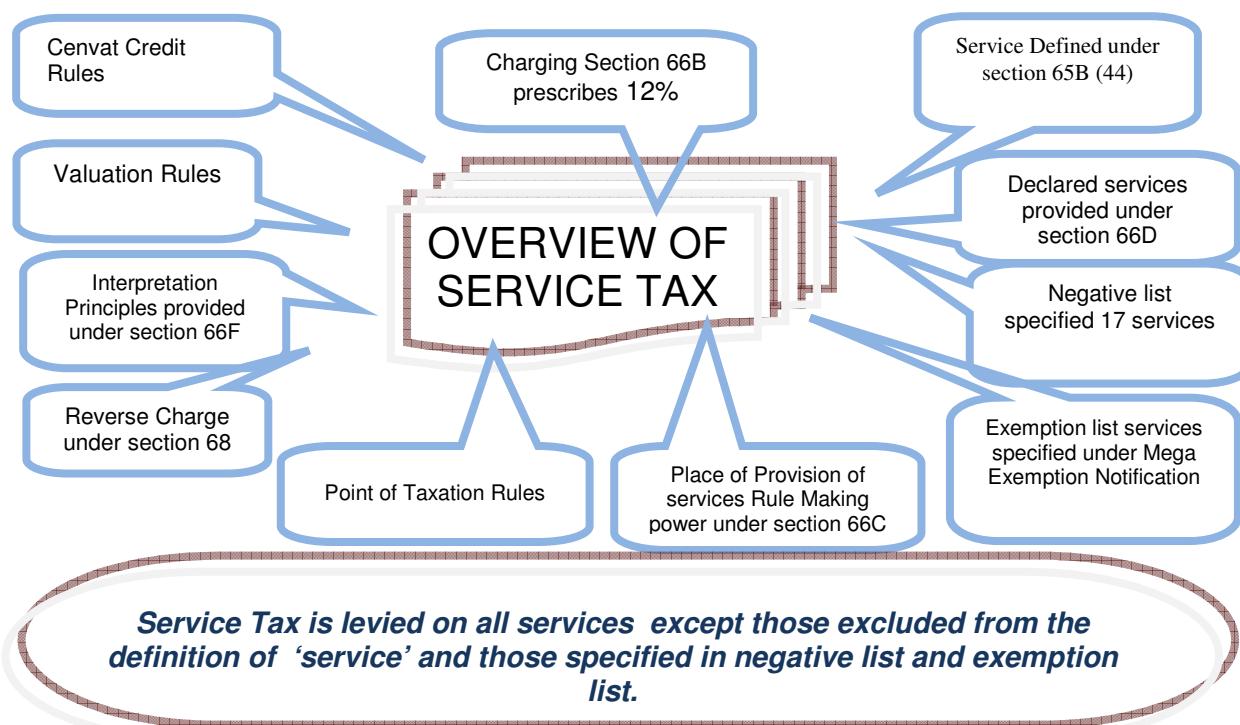
LIMBS OF SERVICE TAX LAWS

The various limbs of the Service Tax Law are:

- Chapter V and VA (SECTIONS 64 TO 98) of the Finance Act, 1994 as amended by successive Finance Acts;
- As per Section 83 of the Finance Act, 1994 the provisions of the following sections of the Central Excise Act, 1944, as in force from time to time, shall apply, so far as may be, in relation to service tax as they apply in relation to a duty of excise :- sub-section 2 of 9A, 9AA, 9B, 9C, 9D, 9E, 11B, 11BB, 11C, 12, 12A, 12B, 12C, 12D, 12E, 14, 15, 31, 32, 32A to 32P, 33A, 35EE, 34A, 35F, 35FF, to 35O (both inclusive), 35Q, 35R, 36, 36A, 36B, 37A, 37B, 37C, 37D 38A and 40. Certain Sections of Central Excise Act, 1944 are also made applicable to the Service Tax matters.
- Service Tax Rules, 1994,
- Service Tax (Advance Ruling), Rules 2003;
- The CENVAT Credit Rules, 2004;
- Service Tax (Advance Rulings) Rules, 2003

- Authority for Advance Rulings (Central Excise, Customs and Service Tax) Procedure Regulations, 2005;
- Service Tax (Registration of Special category of persons) Rules, 2005;
- Service Tax (Determination of Value) Rules, 2006;
- Service Tax (Provisional Attachment of Property) Rules, 2008;
- Service Tax (Publication of Names) Rules, 2008;
- Service Tax Return Preparer Scheme, 2009;
- Point of Taxation Rules, 2011;
- Indirect Tax Ombudsman Guidelines, 2011;
- Service Tax (Settlement of Cases) Rules, 2012;
- Service Tax (Compounding of Offences) Rules, 2012;
- Service Tax (Removal of Difficulty) Order, 2012;
- Place of Provision of Services Rules, 2012.

Further, Service Tax Notifications issued by the Government is also an important limb of Service Tax law. The Central Board of Excise and Customs also issues Circulars on service tax and on the basis of Circulars jurisdictional Commissionerates of Central Excise issues Trade Notices for the guidance of the assessee on service tax matters.



MEANING OF SERVICE

The Finance Act, 2012 has also defined a term “Service” for the first time. In other words, from June 1994 to June 2012, the Finance Act, 1994 was not containing a definition of the term Service.

Clause (44) of Section 65B of the Act has defined a term Service as under:

“Service” means any activity carried out by a person for another for consideration, and includes a declared service, but shall not include—

- (a) an activity which constitutes merely,—
 - (i) a transfer of title in goods or immovable property, by way of sale, gift or in any other manner; or
 - (ii) such transfer, delivery or supply of any goods which is deemed to be a sale within the meaning of clause (29A) of Article 366 of the Constitution; or
 - (iii) a transaction in money or actionable claim;
- (b) a provision of service by an employee to the employer in the course of or in relation to his employment;
- (c) fees taken in any Court or tribunal established under any law for the time being in force.

Explanation 1 — For the removal of doubts, it is hereby declared that nothing contained in this clause shall apply to—

- (A) the functions performed by the Members of Parliament, Members of State Legislative, Members of Panchayats, Members of Municipalities and Members of other local authorities who receive any consideration in performing the functions of that office as such member; or
- (B) the duties performed by any person who holds any post in pursuance of the provisions of the Constitution in that capacity; or
- (C) the duties performed by any person as a Chairperson or a Member or a Director in a body established by the Central Government or State Governments or local authority and who is not deemed as an employee before the commencement of this section.

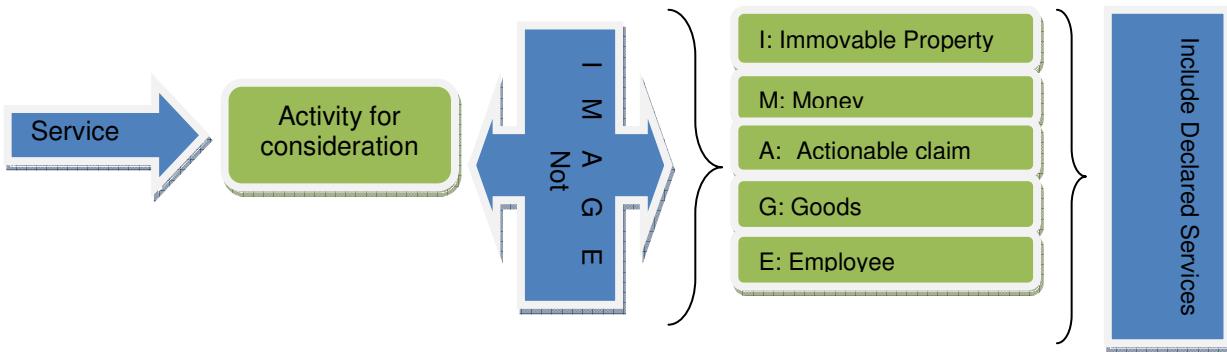
Explanation 2— For the purposes of this clause, transaction in money shall not include any activity relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination to another form, currency or denomination for which a separate consideration is charged.

Explanation 3— For the purposes of this Chapter,—

- (a) an unincorporated association or a body of persons, as the case may be, and a member thereof shall be treated as distinct persons;
- (b) an establishment of a person in the taxable territory and any of his other establishment in a non - taxable territory shall be treated as establishments of distinct persons.

Explanation 4— A person carrying on a business through a branch or agency or representational office in any territory shall be treated as having an establishment in that territory;

Example: Service of an unincorporated body or a non-profit entity registered under any law for the time being in force to its own members up to an amount of ₹5,000 per member per month by way of reimbursement of charges or share of contribution is exempt from service tax. Where RWA is working as a pure agent of its members for sourcing of goods or services from a third person, amount collected by RWA from its members may be excluded from the value of taxable service in terms of Rule 5(2) Of Service Tax (Determination of Value) Rules, 2006 subject to compliance with the specified conditions.



Accounting Codes for Services

Service Tax accounting codes must be mentioned in the Service Tax Payment Challan (GAR 7). In case of Multiple service Provider (a service provider rendering more than one taxable service), amount attributable to each such service along with the concerned accounting codes should be mentioned clearly in the column provided for this purpose in the GAR 7 Challan.

Accounting code for the purpose of payment of service tax under the Negative List approach ["All Taxable Services" – 00441089] was prescribed vide Circular 161/12/2012 dated 6th July, 2012. However, for statistical analysis suggestions were received for restoration of old accounting codes and to provide list of description of services to the taxpayers for obtaining registration. After examining the suggestions old accounting code list has been restored and service specific accounting codes for the purpose of registration and payment of service tax is provided in annexure to the Circular No.165/16/2012 –ST.

(A) DECLARED SERVICES

Section 66E specifies nine activities or transactions which are declared to be covered as 'service'. Such activities include:-

- (a) renting of immovable property
- (b) construction of a complex.
- (c) temporary transfer or permitting the use or enjoyment of any intellectual property right
- (d) development, design, programming, customisation, adaptation, upgradation, enhancement, implementation of information technology software
- (e) agreeing to the obligation to refrain from an act, or to tolerate an act or a situation, or to do an act
- (f) transfer of goods by way of hiring, leasing, licensing or in any such manner without transfer of right to use such goods
- (g) activities in relation to delivery of goods on hire purchase or any system of payment by instalments
- (h) service portion in the execution of a works contract
- (i) service portion in an activity wherein goods, being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as a part of the activity

Para No. 3.4.1 of Taxation of Services – An education Guide dated 20.06.2012 has given the following test to determine whether an activity is a taxable service:

STEP 1: To determine whether service is being provided by you:

S.NO.	QUESTION	Provide Your Answer
1	Am I doing an activity (including, but not limited to, an activity Specified in section 65E of the Act) for another person*?	YES
2	Am I doing such activity for a consideration?	YES
3	Does this activity consist only of transfer of title in goods or immovable property by way of sale, gift or in any other manner?	NO
4	Does this activity constitute only a transfer, delivery or supply of goods which is deemed to be a sale of goods within the meaning of clause (29A) of article 366 of the Constitution?	NO
5	Does this activity consist only of a transaction in money or actionable claim?	NO
6	Is the consideration for the activity in the nature of court fees for a court or a tribunal?	NO
7	Is such an activity in the nature of a service provided by an employee of such person in the course of employment?	NO
8	Is the activity covered in any of the categories specified in Explanation 1 to clause (44) of section 65B of the Act	NO

If the answer to the above questions is as per the above answers in column 3 of the table above THEN you are providing a service.

STEP 2: To determine whether service provided by you is taxable

If you are providing a 'service' (Step 1) and then pose the following Questions to yourself-

S.NO.	QUESTION	ANSWER
1	Have I provided or have I agreed to provide the service?	Yes
	Have I provided or have I agreed to provide the service in the taxable territory?	Yes
2	Is this activity entirely covered in any of the services described in the negative list of services contained in section 66D of the Act?	No

If the answer to the above questions is also as per the answers given in column 2 of the table above then you are providing a 'taxable service'.

(B) NEGATIVE LIST OF SERVICES

A Negative List approach to taxation of services has been introduced vide sections 66B, 66C, 66D, 66E and 66F in Chapter V of the Finance Act. The services specified in the 'Negative List' (section 66D) will remain outside the tax net. All other services, except those specifically exempted by the exercise of powers under

section 93(1) of the Finance Act, 1994, would thus be chargeable to service tax. Negative list approach to taxation of services is effective from July 1, 2012.

Section 66D specify the following list of services under the negative list: –

- (a) services by Government or a local authority excluding the following services to the extent they are not covered elsewhere –
 - (i) services by the Department of Posts by way of speed post, express parcel post, life insurance and agency services provided to a person other than Government.
 - (ii) services in relation to an aircraft or a vessel, inside or outside the precincts of a port or an airport.
 - (iii) transport of goods or passengers.
 - (iv) support services, other than services covered under clauses (i) to (iii) above, provided to business entities.
- (b) services by the Reserve Bank of India.
- (c) services by a foreign diplomatic mission located in India.

services provided by any person for the official use of a foreign diplomatic mission has been exempted vide Notification No. 27/2012 S.T., dated 20.6.2012 subject to prescribed conditions.
- (d) services relating to agriculture or agricultural produce by way of–
 - (i) agricultural operations directly related to production of any agricultural produce including cultivation, harvesting, threshing, plant protection or testing.
 - (ii) supply of farm labour.
 - (iii) processes carried out at an agricultural farm including tending, pruning, cutting, harvesting, drying, cleaning, trimming, sun drying, fumigating, curing, sorting, grading, cooling or bulk packaging and such like operations which do not alter the essential characteristics of agricultural produce but make it only marketable for the primary market.
 - (iv) renting or leasing of agro machinery or vacant land with or without a structure incidental to its use.
 - (v) loading, unloading, packing, storage or warehousing of agricultural produce.
 - (vi) agricultural extension services.
 - (vii) services by any Agricultural Produce Marketing Committee or Board or services provided by a commission agent for sale or purchase of agricultural produce.
- (e) trading of goods.
- (f) any process amounting to manufacture or production of goods.
- (g) selling of space or time slots for advertisements other than advertisements broadcast by radio or television.
- (h) service by way of access to a road or a bridge on payment of toll charges.
- (i) betting, gambling or lottery.
- (j) admission to entertainment events or access to amusement facilities.

- (k) transmission or distribution of electricity by an electricity transmission or distribution utility.
- (l) services by way of –
 - (i) pre-school education and education up to higher secondary school or equivalent.
 - (ii) education as a part of a curriculum for obtaining a qualification recognised by any law for the time being in force.
 - (iii) education as a part of an approved vocational education course.
- (m) services by way of renting of residential dwelling for use as residence.
- (n) services by way of –
 - (i) extending deposits, loans or advances in so far as the consideration is represented by way of interest or discount ;
 - (ii) inter se sale or purchase of foreign currency amongst banks or authorised dealers of foreign exchange or amongst banks and such dealers.
- (o) service of transportation of passengers, with or without accompanied belongings, by
 - (i) a stage carriage
 - (ii) railways in a class other than –
 - (A) first class or
 - (B) an airconditioned coach
 - (iii) metro, monorail or tramway
 - (iv) inland waterways
 - (v) public transport, other than predominantly for tourism purpose, in a vessel between places located in India and
 - (vi) metered cabs, radio taxis or auto rickshaws
- (p) services by way of transportation of goods–
 - (i) by road except the services of–
 - (A) a goods transportation agency; or
 - (B) a courier agency
 - (ii) by an aircraft or a vessel from a place outside India up to the customs station of clearance in India or
 - (iii) by inland waterways
- (q) funeral, burial, crematorium or mortuary services including transportation of the deceased.

(C) LIST OF EXEMPTIONS UNDER MEGA NOTIFICATION

In exercise of the powers conferred by sub-section (1) of section 93 of the Finance Act, 1994, the Central Government has issued Notification No. 25/ 2012 ST dated 20th June 2012 (Mega Exemption Notification) exempting the following taxable services. This notification has come in to effect from 1st day of July, 2012.

1. Services provided to the United Nations or a specified international organization.

“Specified international organization” means an international organization declared by the Central Government in pursuance of section 3 of the United Nations (Privileges and Immunities) Act, 1947 (46 of

1947), to which the provisions of the Schedule to the said Act apply;

The illustrative list of such organizations has been provided by Para No.7.1, Taxation of Services – An Education Guide dated 20.06.2012 as follows:

- *International Civil Aviation Organisation*
- *World Health Organisation*
- *International Labour Organisation*
- *Food and Agriculture Organisation of the United Nations*
- *UN Educational, Scientific and Cultural Organisation (UNESCO)*
- *International Monetary Fund (IMF)*
- *International Bank for Reconstruction and Development*
- *Universal Postal Union*
- *International Telecommunication Union*
- *World Meteorological Organisation*
- *Permanent Central Opium Board*
- *International Hydrographic Bureau*
- *Commissioner for Indus Waters, Government of Pakistan and his advisers and assistants*
- *Asian African Legal Consultative Committee*
- *Commonwealth Asia Pacific Youth Development Centre, Chandigarh*
- *Delegation of Commission of European Community*
- *Customs Co-operation Council*
- *Asia Pacific Telecommunity*
- *International Centre of Public Enterprises in Developing Countries, Ljubljana (Yugoslavia)*
- *International Centre for Genetic Engineering and Biotechnology*
- *Asian Development Bank*
- *South Asian Association for Regional Co-operation*
- *International Jute Organisation, Dhaka, Bangladesh*

2. Health care services by a clinical establishment, an authorized medical practitioner or para-medics.

The terms health care services are defined as follows:

“Health care services” means any service by way of diagnosis or treatment or care for illness, injury, deformity, abnormality or pregnancy in any recognised system of medicines in India and includes

- services by way of transportation of the patient to and from a clinical establishment, but does not include:
- hair transplant or cosmetic or plastic surgery, except when undertaken to restore or to reconstruct anatomy or functions of body affected due to congenital defects, developmental abnormalities, injury or trauma;

As per para 7.2.1 of Taxation of services –An Education Guide the services provided in recognized systems of medicines in India are exempt. In terms of the Clause (h) of section 2 of the Clinical Establishments Act,

2010, the following systems of medicines are recognized systems of medicines:

- *Allopathy*
- *Yoga*
- *Naturopathy*
- *Ayurveda*
- *Homeopathy*
- *Siddha*
- *Unani*
- *Any other system of medicine that may be recognized by central government*

“clinical establishment” means a hospital, nursing home, clinic, sanatorium or any other institution by, whatever name called, that offers services or facilities requiring diagnosis or treatment or care for illness, injury, deformity, abnormality or pregnancy in any recognised system of medicines in India, or a place established as an independent entity or a part of an establishment to carry out diagnostic or investigative services of diseases;

“authorised medical practitioner” means a medical practitioner registered with any of the councils of the recognised system of medicines established or recognized by law in India and includes a medical professional having the requisite qualification to practice in any recognised system of medicines in India as per any law for the time being in force;

Para 7.2.2. of Taxation of services- An Education Guide describes Paramedics are trained health care professionals, for example nursing staff, physiotherapists, technicians, lab assistants etc. Services by them in a clinical establishment would be in the capacity of employee and not provided in independent capacity and will thus be considered as services by such clinical establishment. Similar services in independent capacity are also exempted.

In short, the health care services provided by a clinical establishment, an authorized medical practitioner and paramedics shall be exempt.

- 2A. Services provided by cord blood banks by way of stem cells or any other service in relation to such preservation;
3. Services by a veterinary clinic in relation to health care of animals or birds.
4. Services by an entity registered under section 12AA of the Income tax Act, 1961 (43 of 1961) by way of charitable activities.

“Charitable activities” means activities relating to -

- (i) *public health by way of -*
 - (a) *care or counseling of (i) terminally ill persons or persons with severe physical or mental disability, (ii) persons afflicted with HIV or AIDS, or (iii) persons addicted to a dependence-forming substance such as narcotics drugs or alcohol; or*
 - (b) *public awareness of preventive health, family planning or prevention of HIV infection;*
- (ii) *advancement of religion or spirituality;*
- (iii) *advancement of educational programmes or skill development relating to,-*
 - (a) *abandoned, orphaned or homeless children;*
 - (b) *physically or mentally abused and traumatized persons;*

- (c) prisoners; or
- (d) persons over the age of 65 years residing in a rural area;
- (iv) preservation of environment including watershed, forests and wildlife;

5. Services by a person by way of-

- (a) renting of precincts of a religious place meant for general public; or
- (b) conduct of any religious ceremony.

In this case the exemption is provided to the activity of letting out on rent of areas surrounding, or in the compound of a religious place.

For this purpose, the following are defined as;

"Religious place" means a place which is primarily meant for conduct of prayers or worship pertaining to a religion, meditation, or spirituality;

"General public" means the body of people at large sufficiently defined by some common quality of public or impersonal nature;

6. Services provided by-

- (a) an arbitral tribunal to -
 - (i) any person other than a business entity; or
 - (ii) a business entity with a turnover up to rupees ten lakh in the preceding financial year.

Arbitral tribunal defines as "arbitral tribunal" has the meaning assigned to it in clause (d) of section 2 of the Arbitration and Conciliation Act, 1996 (26 of 1996);

The definition as provided in clause (d) of section 2 of the Arbitration and Conciliation Act, 1996 read as; "arbitral tribunal" means a sole arbitrator or a panel of arbitrators"

Further, Business entity is defined in section 65B of the Finance Act, 1994 as 'any person ordinarily carrying out any activity relating to industry, commerce or any other business.

Thus, services provided by arbitral tribunal to a business entity having turnover of more than ₹ 10 lakhs in the preceding financial year would not be exempt.

- (b) an individual as an advocate or a partnership firm of advocates by way of legal services to,-
 - (i) an advocate or partnership firm of advocates providing legal services ;
 - (ii) any person other than a business entity; or
 - (iii) a business entity with a turnover up to rupees ten lakh in the preceding financial year; or

"Advocate" has the meaning assigned to it in clause (a) of sub-section (1) of section 2 of the Advocates Act, 1961 (25 of 1961);

The definition of advocate has been defined in clause (a) of subsection (1) of section of the Advocates Act, 1961 as; "advocate means an advocate entered in any roll under the provisions of this Act"

"legal service" means any service provided in relation to advice, consultancy or assistance in any

branch of law, in any manner and includes representational services before any court, tribunal or authority;

Thus, any services provided by such advocates/firms in fields other than legal services would be taxable. Such services can include services relating to mergers and acquisitions, due diligence etc.

- (c) a person represented on an arbitral tribunal to an arbitral tribunal.

7. Services by way of technical testing or analysis of newly developed drugs, including vaccines and herbal remedies, on human participants by a clinical research organisation approved to conduct clinical trials by the Drug Controller General of India.

In order to promote development of new drugs, exemption is provided to testing and analysis of such new drugs.

8. Services by way of training or coaching in recreational activities relating to arts, culture or sports.

Vide Circular No. 164/15/2012 S.T, dated 28-08-2012, it has been clarified that no service tax is leviable on vocational education/training/skill development courses (VEC) offered by the Government (Central Government or state Government) or local authority themselves. Also in case of such courses offered by an entity independently established by the Government under the law as a society or any other similar body, it has been clarified that the words "recognised by an entity established under a central or state law including delegated legislation, for the purpose of granting recognition to any education course including a VEC

9. Services provided to an educational institution in respect of education exempted from service tax, by way of,-

- (a) auxiliary educational services; or
- (b) renting of immovable property.

Here, exemption is provided to

- to an educational institution
- in respect of education
- which is exempt from levy of service tax
- by way of auxiliary educational services
- by way of renting of immovable property.

For this purpose 'auxiliary educational services' are defined as follows:

"auxiliary educational services" means any services relating to imparting any skill, knowledge, education or development of course content or any other knowledge – enhancement activity, whether for the students or the faculty, or any other services which educational institutions ordinarily carry out themselves but may obtain as outsourced services from any other person, including services relating to admission to such institution, conduct of examination, catering for the students under any mid-day meals scheme sponsored by Government, or transportation of students, faculty or staff of such institution;

9A. Any services provided by, _

- (i) the National Skill Development Corporation set up by the Government of India;
- (ii) a Sector Skill Council approved by the National Skill Development Corporation;

- (iii) an assessment agency approved by the Sector Skill Council or the National Skill Development Corporation;
- (iv) a training partner approved by the National Skill Development Corporation or the Sector Skill Council in relation to (a) the National Skill Development Programme implemented by the National Skill Development Corporation; or (b) a vocational skill development course under the National Skill Certification and Monetary Reward Scheme; or (c) any other Scheme implemented by the National Skill Development Corporation.

10. Services provided to a recognised sports body by-

- (a) an individual as a player, referee, umpire, coach or team manager for participation in a sporting event organized by a recognized sports body;
- (b) another recognised sports body.

“Recognized sports body” means - (i) the Indian Olympic Association, (ii) Sports Authority of India, (iii) a national sports federation recognised by the Ministry of Sports and Youth Affairs of the Central Government, and its affiliate federations, (iv) national sports promotion organisations recognised by the Ministry of Sports and Youth Affairs of the Central Government, (v) the International Olympic Association or a federation recognised by the International Olympic Association or (vi) a federation or a body which regulates a sport at international level and its affiliated federations or bodies regulating a sport in India;

For this purpose ‘Recognized sports body’ is defined as follows:

11. Services by way of sponsorship of sporting events organised,-

- (a) by a national sports federation, or its affiliated federations, where the participating teams or individuals represent any district, state, zone; or country;
- (b) by Association of Indian Universities, Inter-University Sports Board, School Games Federation of India, All India Sports Council for the Deaf, Paralympic Committee of India or Special Olympics Bharat;
- (c) by Central Civil Services Cultural and Sports Board;
- (d) as part of national games, by Indian Olympic Association; or
- (e) under Panchayat Yuva Kreedha Aur Khel Abhiyaan (PYKKA) Scheme.

12. Services provided to the Government, a local authority or a governmental authority by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration of-

- (a) a civil structure or any other original works meant predominantly for use other than for commerce, industry, or any other business or profession;
- (b) a historical monument, archaeological site or remains of national importance, archaeological excavation, or antiquity specified under the Ancient Monuments and Archaeological Sites and Remains Act, 1958 (24 of 1958);
- (c) a structure meant predominantly for use as (i) an educational, (ii) a clinical, or (iii) an art or cultural establishment;
- (d) canal, dam or other irrigation works;
- (e) pipeline, conduit or plant for (i) water supply (ii) water treatment, or (iii) sewerage treatment or disposal; or

- (f) a residential complex predominantly meant for self-use or the use of their employees or other persons specified in the Explanation 1 to clause 44 of section 65 B of the said Act.

For this purpose 'governmental authority' is defined as follows:

"governmental authority" means a board, or an authority or any other body established with 90% or more participation by way of equity or control by Government and set up by an Act of the Parliament or a State Legislature to carry out any function entrusted to a municipality under article 243W of the Constitution;

13. Services provided by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration of,-

- (a) a road, bridge, tunnel, or terminal for road transportation for use by general public;
- (b) a civil structure or any other original works pertaining to a scheme under Jawaharlal Nehru National Urban Renewal Mission or Rajiv Awaas Yojana;
- (c) a building owned by an entity registered under section 12AA of the Income tax Act, 1961(43 of 1961) and meant predominantly for religious use by general public;
- (d) a pollution control or effluent treatment plant, except located as a part of a factory; or
- (e) a structure meant for funeral, burial or cremation of deceased.

14. Services by way of construction, erection, commissioning, or installation of original works pertaining to,-

- (a) an airport, port or railways, including monorail or metro;
- (b) a single residential unit otherwise than as a part of a residential complex;
- (c) low-cost houses up to a carpet area of 60 square metres per house in a housing project approved by competent authority empowered under the 'Scheme of Affordable Housing in Partnership' framed by the Ministry of Housing and Urban Poverty Alleviation, Government of India;
- (d) post-harvest storage infrastructure for agricultural produce including a cold storages for such purposes; or
- (e) mechanised food grain handling system, machinery or equipment for units processing agricultural produce as food stuff excluding alcoholic beverages.

"Original works" means has the meaning assigned to it in Rule 2A of the Service Tax (Determination of Value) Rules, 2006;

Definition as provided in such rules is as follows:

Original works means:

- (i) All new constructions;
- (ii) All types of additions and alterations to abandoned or damaged structures on land that are required to make them workable;
- (iii) Erection, commissioning or installation of plant, machinery or equipment or structures, whether pre-fabricated or otherwise.

"residential complex" means any complex comprising of a building or buildings, having more than one single residential unit;

"single residential unit" means a self-contained residential unit which is designed for use, wholly or principally, for residential purposes for one family;

15. Services provided by way of temporary transfer or permitting the use or enjoyment of a copyright,-

- (a) covered under clause (a) of sub-section (1) of section 13 of the Copyright Act, 1957 (14 of 1957), relating to original literary, dramatic, musical or artistic works; or
- (b) of cinematograph films for exhibition in a cinema hall or cinema theatre.

16. Services by a performing artist in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, excluding services provided by such artist as a brand ambassador.

17. Services by way of collecting or providing news by an independent journalist, Press Trust of India or United News of India.

18. Services by way of renting of a hotel, inn, guest house, club, campsite or other commercial places meant for residential or lodging purposes, having declared tariff of a unit of accommodation below rupees one thousand per day or equivalent.

"Declared tariff" includes charges for all amenities provided in the unit of accommodation (given on rent for stay) like furniture, air-conditioner, refrigerators or any other amenities, but without excluding any discount offered on the published charges for such unit;

19. Services provided in relation to serving of food or beverages by a restaurant, eating joint or a mess, other than those having the facility of air-conditioning or central air-heating in any part of the establishment, at any time during the year.

19A. Services provided in relation to serving of food or beverages by a canteen maintained in a factory covered under the Factories Act, 1948 (63 of 1948), having the facility of air-conditioning or central air-heating at any time during the year

20. Services by way of transportation by rail or a vessel from one place in India to another of the following goods -

- (a) omitted by Finance Act, 2013 as enacted on 10th May 2013;
- (b) relief materials meant for victims of natural or man-made disasters, calamities, accidents or mishap;
- (c) defence or military equipments;
- (d) omitted;
- (e) omitted;
- (f) newspaper or magazines registered with the Registrar of Newspapers;
- (g) railway equipments or materials;
- (h) agricultural produce;
- (i) foodstuff including flours, tea, coffee, jaggery, sugar, milk products, salt and edible oil, excluding alcoholic beverages; or
- (j) chemical fertilizer and oilcakes.

21. Services provided by a goods transport agency, by way of transport in a goods carriage of,-

- (a) agricultural produce;
- (b) goods, where gross amount charged for the transportation of goods on a consignment transported in a single carriage does not exceed one thousand five hundred rupees;
- (c) goods, where gross amount charged for transportation of all such goods for a single consignee

- does not exceed rupees seven hundred fifty;
- (d) foodstuff including flours, tea, coffee, jaggery, sugar, milk products, salt and edible oil, excluding alcoholic beverages;
 - (e) chemical fertilizer and oilcakes;
 - (f) newspaper or magazines registered with the Registrar of Newspapers;
 - (g) relief materials meant for victims of natural or man-made disasters, calamities, accidents or mishap; or
 - (h) defence or military equipments;

“Goods carriage” has the meaning assigned to it in clause (14) of section 2 of the Motor Vehicles Act, 1988 (59 of 1988);

22. Services by way of giving on hire -

- (a) to a state transport undertaking, a motor vehicle meant to carry more than twelve passengers; or
- (b) to a goods transport agency, a means of transportation of goods.

“State transport undertaking” has the meaning assigned to it in clause (42) of section 2 of the Motor Vehicles Act, 1988 (59 of 1988);

For clarification, *Taxation of services –An Education Guide dated 20.06.2012, provides the following:*

7.11.5 Is giving of a bus on hire to any person liable to tax?

Giving on hire a bus to a state transport undertaking is exempt from service tax. If the bus is given on hire to a person other than a state transport undertaking, it will be taxed.

23. Transport of passengers, with or without accompanied belongings, by -

- (a) air, embarking from or terminating in an airport located in the state of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, or Tripura or at Bagdogra located in West Bengal;
- (b) a contract carriage for the transportation of passengers, excluding tourism, conducted tour, charter or hire; or
- (c) ropeway, cable car or aerial tramway.

“contract carriage” has the meaning assigned to it in clause (7) of section 2 of the Motor Vehicles Act, 1988 (59 of 1988);

24. Omitted;

25. Services provided to Government, a local authority or a governmental authority by way of -

- (a) carrying out any activity in relation to any function ordinarily entrusted to a municipality in relation to water supply, public health, sanitation conservancy, solid waste management or slum improvement and upgradation; or
- (b) repair or maintenance of a vessel.

26 Services of general insurance business provided under following schemes-

- (a) Hut Insurance Scheme;
- (b) Cattle Insurance under Swarnajayanti Gram Swarozgar Yojna (earlier known as Integrated Rural

- Development Programme);
- (c) Scheme for Insurance of Tribals;
 - (d) Janata Personal Accident Policy and Gramin Accident Policy;
 - (e) Group Personal Accident Policy for Self-Employed Women;
 - (f) Agricultural Pumpset and Failed Well Insurance;
 - (g) premia collected on export credit insurance;
 - (h) Weather Based Crop Insurance Scheme or the Modified National Agricultural Insurance Scheme, approved by the Government of India and implemented by the Ministry of Agriculture;
 - (i) Jan Arogya Bima Policy;
 - (j) National Agricultural Insurance Scheme (Rashtriya Krishi Bima Yojana);
 - (k) Pilot Scheme on Seed Crop Insurance;
 - (l) Central Sector Scheme on Cattle Insurance;
 - (m) Universal Health Insurance Scheme;
 - (n) Rashtriya Swasthya Bima Yojana; or
 - (o) Coconut Palm Insurance Scheme.

26A. Services of life insurance business provided under the following schemes-

- (a) Janashree Bima Yojana (JBY); or
- (b) Aam Aadmi Bima Yojana (AABY);

27. Services provided by an incubatee up to a total turnover of fifty lakh rupees in a financial year subject to the following conditions, namely:-

- (a) the total turnover had not exceeded fifty lakh rupees during the preceding financial year; and
- (b) a period of three years has not been elapsed from the date of entering into an agreement as an incubatee.

“incubatee” means an entrepreneur located within the premises of a Technology Business Incubator (TBI) or Science and Technology Entrepreneurship Park (STEP) recognised by the National Science and Technology Entrepreneurship Development Board (NSTEDB) of the Department of Science and Technology, Government of India and who has entered into an agreement with the TBI or the STEP to enable himself to develop and produce hi-tech and innovative products;

28. Service by an unincorporated body or a non- profit entity registered under any law for the time being in force, to its own members by way of reimbursement of charges or share of contribution -

- (a) as a trade union;
- (b) for the provision of carrying out any activity which is exempt from the levy of service tax; or
- (c) up to an amount of five thousand rupees per month per member for sourcing of goods or services from a third person for the common use of its members in a housing society or a residential complex;

“trade union” has the meaning assigned to it in clause (h) of section 2 of the Trade Unions Act, 1926 (16 of 1926).

For clarification Taxation of services – An Education Guide dated 20.06.2012, provides the following:

7.11.9 I am a Resident Welfare Association (RWA). The members contribute an amount to RWA for holding

camps to provide health care services to poor men and women. Am I required to pay tax on contribution received from members?

No. You are not required to pay service tax on the contribution received as you are carrying out any activity (holding camps to provide health care services) which is exempt from the levy of service tax. If contribution is for carrying out an activity which is taxable, you are required to pay service tax.

29. Services by the following persons in respective capacities -

- (a) sub-broker or an authorised person to a stock broker;
- (b) authorised person to a member of a commodity exchange;
- (c) mutual fund agent to a mutual fund or asset management company;
- (d) distributor to a mutual fund or asset management company;
- (e) selling or marketing agent of lottery tickets to a distributor or a selling agent;
- (f) selling agent or a distributor of SIM cards or recharge coupon vouchers;
- (g) business facilitator or a business correspondent to a banking company or an insurance company, in a rural area; or
- (h) sub-contractor providing services by way of works contract to another contractor providing works contract services which are exempt;

“sub-broker” has the meaning assigned to it in sub-clause (gc) of clause 2 of the Securities and Exchange Board of India (Stock Brokers and Sub-brokers) Regulations, 1992;

“authorised person” means any person who is appointed as such either by a stock broker (including trading member) or by a member of a commodity exchange and who provides access to trading platform of a stock exchange or a commodity exchange as an agent of such stock broker or member of a commodity exchange;

“commodity exchange” means an association as defined in section 2(j) and recognized under section 6 of the Forward Contracts (Regulation) Act, 1952 (74 of 1952);

“distributor or selling agent” has the meaning assigned to them in clause (c) of the rule 2 of the Lottery (Regulation) Rules, 2010 notified by the Government of India in the Ministry of Home Affairs, published in the Gazette of India, Extraordinary, Part-II, Section 3, Sub-section (i), vide number G.S.R. 278(E), dated the 1st April, 2010 and shall include distributor or selling agent authorised by the lottery-organising State;

“business facilitator or business correspondent” means an intermediary appointed under the business facilitator model or the business correspondent model by a banking company or an insurance company under the guidelines issued by Reserve Bank of India;

“banking company” has the meaning assigned to it in clause (a) of section 45A of the Reserve Bank of India Act, 1934(2 of 1934);

“general insurance business” has the meaning assigned to it in clause (g) of section 3 of General Insurance Business (Nationalisation) Act, 1972 (57 of 1972);

“insurance company” means a company carrying on life insurance business or general insurance business;

“life insurance business” has the meaning assigned to it in clause (11) of section 2 of the Insurance Act, 1938 (4 of 1938);

"rural area" means the area comprised in a village as defined in land revenue records, excluding- the area under any municipal committee, municipal corporation, town area committee, cantonment board or notified area committee; or any area that may be notified as an urban area by the Central Government or a State Government;

For clarification *Taxation of services –An Education Guide dated 20.06.2012*, provides the following:

2.8.12 Would recharge vouchers issued by service companies for enabling clients/consumers to avail services like mobile phone communication, satellite TV broadcasts, DTH broadcasts etc be 'actionable claims'?

No. Such recharge vouchers do not create a 'beneficial interest' in a moveable property but only enable a person to enjoy a particular service.

7.11.11 Whether the exemption provided in the mega -exemption to services by way of construction of roads, airports, railways, transport terminals, bridges, tunnels, dams etc., is also available to the sub-contractors who provide input service to these main contractors in relation to such construction?

As per clause (1) of section 66F reference to a service by nature or description in the Act will not include reference to a service used for providing such service. Therefore, if any person is providing services, in respect of projects involving construction of roads, airports, railways, transport terminals, bridges, tunnels, dams etc., such as architect service, consulting engineer service ., which are used by the contractor in relation to such construction, the benefit of the specified entries in the mega-exemption would not be available to such persons unless the activities carried out by the sub-contractor independently and by itself falls in the ambit of the exemption.

It has to be appreciated that the wordings used in the exemption are 'services by way of construction of roads etc' and not 'services in relation to construction of roads etc'. It is thus apparent that just because the main contractor is providing the service by way of construction of roads, airports, railways, transport terminals, bridges, tunnels, dams etc., it would not automatically lead to the classification of services being provided by the sub-contractor to the contractor as an exempt service.

However, a sub-contractor providing services by way of works contract to the main contractor, providing exempt works contract services, has been exempted from service tax under the mega exemption if the main contractor is engaged in providing exempt services of works contracts. It may be noted that the exemption is available to sub-contractors engaged in works contracts and not to other outsourced services such as architect or consultants.

30. Carrying out an intermediate production process as job work in relation to -

- (a) agriculture, printing or textile processing;
- (b) cut and polished diamonds and gemstones; or plain and studded jewellery of gold and other precious metals, falling under Chapter 71 of the Central Excise Tariff Act ,1985 (5 of 1986);
- (c) any goods on which appropriate duty is payable by the principal manufacturer; or
- (d) processes of electroplating, zinc plating, anodizing, heat treatment, powder coating, painting including spray painting or auto black, during the course of manufacture of parts of cycles or sewing machines upto an aggregate value of taxable service of the specified processes of one hundred and fifty lakh rupees in a financial year subject to the condition that such aggregate value had not exceeded one hundred and fifty lakh rupees during the preceding financial year;

"Appropriate duty" means duty payable on manufacture or production under a Central Act or a State Act, but shall not include 'Nil' rate of duty or duty wholly exempt;

"Principal manufacturer" means any person who gets goods manufactured or processed on his account from another person;

31. Services by an organiser to any person in respect of a business exhibition held outside India;

For clarification Taxation of services –An Education Guide dated 20.06.2012, provides the following:

Para No. 7.11.16 Footwear Association of India is organizing a business exhibition in Germany for footwear manufacturers of India. Is Footwear association of India required to pay service tax on services to footwear manufacturers?

No. The activity is exempt from service tax.

32. Services by way of making telephone calls from -

- (a) departmentally run public telephone;
- (b) guaranteed public telephone operating only for local calls; or
- (c) free telephone at airport and hospital where no bills are being issued.

For clarification Taxation of services –An Education Guide dated 20.06.2012, provides the following:

Para No. 7.11.13 Whether service tax is leviable on telephone services rendered by M/s. BSNL through Village Panchayat Telephone (VPT) with local call facility, as M/s. BSNL is a public sector unit and telephones run by it cannot be treated as 'departmentally run telephones'?

As per Sl. No. 32 of the mega-exemption Notification in addition to exemption to 'departmentally run telephones' there is exemption for 'Guaranteed Public Telephone operating only for local calls' also. Village Public Telephones (VPTs) with facility of local calls (without 9 dialing facility or STD facility) run by BSNL would fall under the category of 'Guaranteed Public Telephone operating only for local calls'.

33. Services by way of slaughtering of animals.

34. Services received from a provider of service located in a non- taxable territory by -

- (a) Government, a local authority, a governmental authority or an individual in relation to any purpose other than commerce, industry or any other business or profession;
- (b) an entity registered under section 12AA of the Income tax Act, 1961 (43 of 1961) for the purposes of providing charitable activities; or
- (c) a person located in a non-taxable territory.

For clarification Taxation of services –An Education Guide dated 20.06.2012, provides the following example:

Para No. 7.11.17 I am resident in Jammu and Kashmir and planning to construct a property in Delhi. I have got the architectural drawings made from an architect who is also resident in Jammu and Kashmir. Am I liable to pay service tax on architect services?

Solution: No. Even though the property is located in Delhi- in a taxable territory- your architect is exempt from service tax as both the service provider and the service receiver is in a non-taxable territory.

35. Services of public libraries by way of lending of books, publications or any other knowledge- enhancing content or material.

36. Services by Employees' State Insurance Corporation to persons governed under the Employees'

Insurance Act, 1948 (34 of 1948).

37. Services by way of transfer of a going concern, as a whole or an independent part thereof.

As per Taxation of services –An Education Guide dated 20.06.2012, 'transfer of going concern' means transfer of a running business which is capable of being carried on by the purchaser as an independent business, but shall not cover mere or predominant transfer of an activity comprising a service. Such sale of business as a whole will comprise comprehensive sale of immovable property, goods and transfer of unexecuted orders, employees, goodwill etc. Since the transfer in title is not merely a transfer in title of either the immovable property or goods or even both it may amount to service and has thus been exempted.

38. Services by way of public conveniences such as provision of facilities of bathroom, washrooms, lavatories, urinal or toilets.

39. Services by a governmental authority by way of any activity in relation to any function entrusted to a municipality under article 243W of the Constitution.

40. Services by way of loading, unloading, packing, storage or warehousing of rice.

“governmental authority” means an authority or a board or any other body;

- (i) set up by an Act of the Parliament or a State Legislature; or
- (ii) established by Government, with 90% or more participation by way of equity or control, to carry out any function entrusted to a municipality under article 243W of the Constitution;

(D) PLACE OF PROVISION OF SERVICES RULES

Service Tax Is Destination Consumption Based Tax

Service Tax is a Value Added Tax (VAT) and is destination based consumption tax in the sense that it is on commercial activities and is not a charge on the business but on the consumer and it would, logically, be leviable only on services provided within the country. This principle is more or less universally applied.

In terms of this principle, exports are not charged to tax, as the consumption is outside the taxable territory, and services are taxed on their importation into the taxable territory.

However, most of the services are intangible in nature; the determination of place of their consumption is not easy. Services could be provided by a person located at one location, actually performed at another while being delivered to a person located at a third location, and occasionally actually consumed at a third location or over a larger geographical territory, falling in more than one taxable jurisdiction. For example a person situated in Delhi may buy a ticket on line from a service provider located outside India, say Delta Airline, USA for a journey from Mumbai to New York, wherein part of the service will be provided on Indian land mass or in taxable territory (the territory of India including territorial waters of India extending up to 12 nautical miles (under International Sea Act). Hence services provided beyond the territorial waters of India are not liable to service tax as the provisions of the service tax have not been extended beyond India). On other occasions the exact location of service recipient itself may not be available e.g. services supplied electronically through internet such as software services, web based services, software maintenance services. As a result it is necessary to lay down rules determining the exact place of provision, while ensuring a certain level of harmonization with international practices in order to avoid both the double taxation as well as double non-taxation of services.

It is also a common practice to largely tax services provided by business to other business entities, based on the location of the customers and other services from business to consumers based on the location of the service provider. Since the determination in terms of above principle is not easy, or sometimes not

practicable, nearest proxies are adopted to provide specificity in the interpretation as well as application of the law.

Function of Place of Provision of Services Rules, 2012

These rules are primarily meant for:

- (a) The assessee who deal in cross-border services (from taxable territory to non taxable territory or from non taxable territory to taxable territory).
- (b) Those assessees who have operations with suppliers or customers in the state of Jammu and Kashmir.
- (c) Service providers operating within India (within the taxable territory) from multiple locations, without having centralized registration will find them useful in determining the precise taxable jurisdiction applicable to their operations.
- (d) Determining services that are wholly consumed within a SEZ, to avail the outright exemption from service tax.

Basic Framework

Place of Provision of Services (POPS) Rules, 2012 are comprehensive set of rules which provides for whether a service has been provided in taxable territory or not. The concept of Export or Import service has been replaced with provision of service in taxable or non taxable territory and therefore no separate set of rules for Export and Import of services exists. The rules for determination of import of services has done away with and export of services are now determined with Rule 6A of Service Tax Rules, 1994.

How the POPS Rules, 2012 shall apply

The answer to this question is provided in Para 5.2.1. of Taxation of Services – An Education Guide dated 20.06.2012 as follows:

As stated earlier, in terms of section 66B, a service is taxable only when, *inter alia*, it is “provided (or agreed to be provided) in the taxable territory”. Thus, the taxability of a service will be determined based on the place of its provision. For determining the taxability of a service, therefore, one needs to ask the following questions sequentially:-

1. Which rule applies to the service provided specifically? In case more than one rules apply equally, which of these come later in the order given in the rules?
2. What is the place of provision of the service in terms of the above rule?
3. Is the place of provision in taxable territory? If yes, tax will be payable. If not, tax will not be payable.
4. Is the provider ‘located’ in the taxable territory? If yes, he will pay the tax.
5. If not, is the service receiver located in taxable territory? If yes, he may be liable to pay tax on reverse charge basis.
6. Is the service receiver an individual or government receiving services for a non business purpose, or a charity receiving services for a charitable activity? If yes, the same is exempted. If not, he is liable to pay tax.

Before moving to the Rules for determining the Place of provision of Services Rules, the understanding of the following term is very important.

Taxable territory has been defined in sub-section 52 of section 65B. It means the territory to which the provisions of Chapter V of the Finance Act, 1994 apply i.e. whole of India excluding the state of Jammu and Kashmir.

“Non-taxable territory” is defined in sub-section 35 *ibid* accordingly as the territory other than the taxable territory.

“India” is defined in sub-section 27 of section 65 B, as follows:

“India” means—

- (a) the territory of the Union of India as referred to in clauses (2) and (3) of article 1 of the Constitution;
- (b) its territorial waters, continental shelf, exclusive economic zone or any other maritime zone as defined in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and Other Maritime Zones Act, 1976;
- (c) the sea-bed and the subsoil underlying the territorial waters;
- (d) the air space above its territory and territorial waters; and
- (e) the installations structures and vessels located in the continental shelf of India and the exclusive economic zone of India, for the purposes of prospecting or extraction or production of mineral oil and natural gas and supply thereof;

Order of Application of POPS, Rules 2012

Rule 14 of POPS rules, provides that rules should be interpreted in reverse order, means rules which comes last in order will be considered first and if that is not applicable then go to the second last and so on. These rules should be applied in the reverse order (from below to above) i.e. in case rule 8 is applicable no other rule prior to this rule shall be applicable.

An illustration is given in Para 5.14.1 of Taxation of Services – An Education Guide dated 20.06.2012 as follows:

Illustration 1

An architect based in Mumbai provides his service to an Indian Hotel Chain (which has business establishment in New Delhi) for its newly acquired property in Dubai. If Rule 5 (Property rule) were to be applied, the place of provision would be the location of the property i.e. Dubai (outside the taxable territory). With this result, the service would not be taxable in India. Whereas, by application of Rule 8, since both the provider and the receiver are located in taxable territory, the place of provision would be the location of the service receiver i.e. New Delhi. Place of provision being in the taxable territory, the service would be taxable in India.

By application of Rule 14, the later of the Rules i.e. Rule 8 would be applied to determine the place of provision.

Illustration 2

For the Ms Universe Contest planned to be held in South Africa, the Indian pageant (say, located in Mumbai) avails the services of Indian beauticians, fashion designers, videographers, and photographers. The service providers travel as part of the Indian pageant's entourage to South Africa. Some of these services are in the nature of personalized services, for which the place of provision would normally be the location where performed (Performance rule-Rule 4), while for others, under the main rule (Receiver location) the place of provision would be the location of receiver.

Whereas, by application of Rule 8, since both the provider and the receiver are located in taxable territory, the place of provision would be the location of the service receiver i.e. New Delhi. Place of provision being in the taxable territory, the service would be taxable in India.

By application of Rule 14, the later of the Rules i.e. Rule 8 would be applied to determine the place of provision.

Main Rule: Rule 3

Rule 3 of the POPS rules provide the basic rule (except provided otherwise in the POPS Rules). As per this rule, the place of provision of services shall be:

- the location of the recipient of service
- in case the location of the service receiver is not available in the ordinary course of business, the place of provision shall be the location of the provider of service.

The principal effect of this rule is that:-

- A. Where the location of receiver of a service is in the taxable territory, such service will be deemed to be provided in the taxable territory and service tax will be payable.
- B. However if the receiver is located outside the taxable territory, no service tax will be payable on the said service.

Rule 2 defines 'location of service provider' as follows:

- (h) "location of the service provider" means-
- (a) where the service provider has obtained a single registration, whether centralized or otherwise, the premises for which such registration has been obtained;
 - (b) where the service provider is not covered under sub-clause (a):
 - (i) *the location of his business establishment; or*
 - (ii) *where the services are provided from a place other than the business establishment, that is to say, a fixed establishment elsewhere, the location of such establishment; or*
 - (iii) *where services are provided from more than one establishment, whether business or*
 - (iv) *fixed, the establishment most directly concerned with the provision of the service; and in the absence of such places, the usual place of residence of the service provider.*

Rule 2 defines 'location of service receiver' as follows

- (i) "Location of the service receiver" means:-
- (a) where the recipient of service has obtained a single registration, whether centralized or otherwise, the premises for which such registration has been obtained;
 - (b) where the recipient of service is not covered under sub-clause (a):
 - (i) the location of his business establishment; or
 - (ii) where services are used at a place other than the business establishment, that is to say, a fixed establishment elsewhere, the location of such establishment; or
 - (iii) where services are used at more than one establishment, whether business or fixed, the establishment most directly concerned with the use of the service; and
 - (iv) in the absence of such places, the usual place of residence of the recipient of service.

Explanation:- For the purposes of clauses (h) and (i), "usual place of residence" in case of a body corporate means the place where it is incorporated or otherwise legally constituted.

Explanation 2:- For the purpose of clause (i), in the case of telecommunication service, the usual place of residence shall be the billing address.

Who is a service receiver?

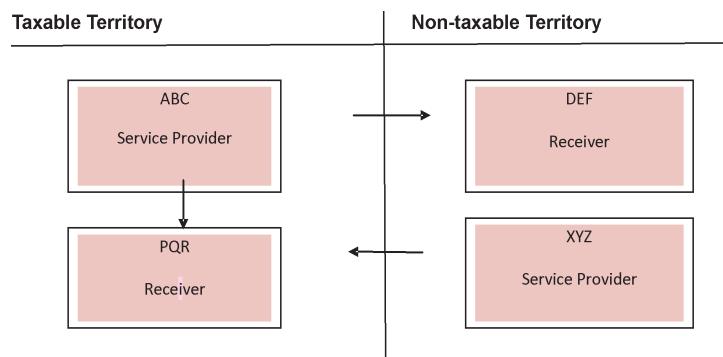
Para 5.3.3 of Taxation of Services – An Education Guide dated 20.06.2012 provides as follows:

Normally, the person who is legally entitled to receive a service and, therefore, obliged to make payment, is the receiver of a service, whether or not he actually makes the payment or someone else makes the payment on his behalf.

Service tax is normally required to be paid by the provider of a service, except where he is located outside the taxable territory and the place of provision of service is in the taxable territory.

Where the provider of a service is located outside the taxable territory, the person liable to pay service tax is the receiver of the service in the taxable territory, unless of course, the service is otherwise exempted.

Following illustration will make this clear:-



A company ABC provides a service to a receiver PQR, both located in the taxable territory. Since the location of the receiver is in the taxable territory, the service is taxable. Service tax liability will be discharged by ABC, being the service provider and being located in taxable territory.

However, if ABC were to supply the same service to a recipient DEF located in non-taxable territory, the provision of such service is not taxable, since the receiver is located outside the taxable territory.

If the same service were to be provided to PQR (located in taxable territory) by an overseas provider XYZ (located in non-taxable territory), the service would be taxable, since the recipient is located in the taxable territory. However, since the service provider is located in a non-taxable territory, the tax liability would be discharged by the receiver, under the reverse charge principle (also referred to as "tax shift").

RATE OF SERVICE TAX

The rate of service tax is mentioned in the charging section. As per the new charging section 66B, as stated earlier, service tax is leviable @12% on the value of taxable services. Further, as per section 91 read with section 95 of the Finance (No. 2) Act, 2004 Section education cess is leviable @ 2% and as per section 136 read with section 140 of the Finance Act, 2007 secondary and higher education cess is leviable @ of on the amount of Service Tax levied. Education cess of 2% and secondary and higher education cess of 1% is in the nature of sur tax on service tax.

Computation of Service Tax

If a person renders a taxable service of the value of ₹ 500, the service tax @12% will be ₹ 60. The Education cess of 2% on ₹ 60 will be ₹ 1.20 and secondary and higher education cess of 1% will be ₹ 0.60. Thus, a total tax will be ₹ 61.80.

ROUNDING OFF OF SERVICE TAX

The provisions of Section 37D of the Central Excise Act, 1944 are applicable to Service Tax Law by virtue of Section 83 of Finance Act, 1994 (as amended), provide that the amount of service tax, interest, penalty, fine or any other sum payable and the amount of refund or any other sum due, under the provisions shall be rounded off to the nearest rupee and, for this purpose, where such amount contains a part of a rupee consisting of paise then, if such part is fifty paise or more, it shall be increased to one rupee and if such part is less than fifty paise it shall be ignored.

LESSON ROUND UP

- The Tax Reform Committee headed by Dr. Raja C. Chelliah recognised the revenue potential of service sector and recommended imposition of service tax on some select services.
- Entry No. 92C has not yet been made effective by the parliament and service tax is still governed by the entry 97 of the union list.
- The Central Board of Excise and Customs has been entrusted with the task of administration of service tax.
- The taxation of services is completely overhauled from positive approach or selective services to negative list approach. Now, no classification of services is required for the purpose of taxability.
- With the introduction of Negative list approach the services which are out of the purview of negative list and mega exemption list are chargeable to service tax.
- Services rendered in taxable territory are taxable for which Place of Provision of Service Rules, 2012 ('PPSR') are prescribed and with this Import of services and export of services rules has been rescinded.
- Service tax is charged @12% plus Education cess @2% and SHEC @ 1%.
- Service tax, interest, fine, penalty or any other sum payable shall be rounded off to the nearest of rupee one.

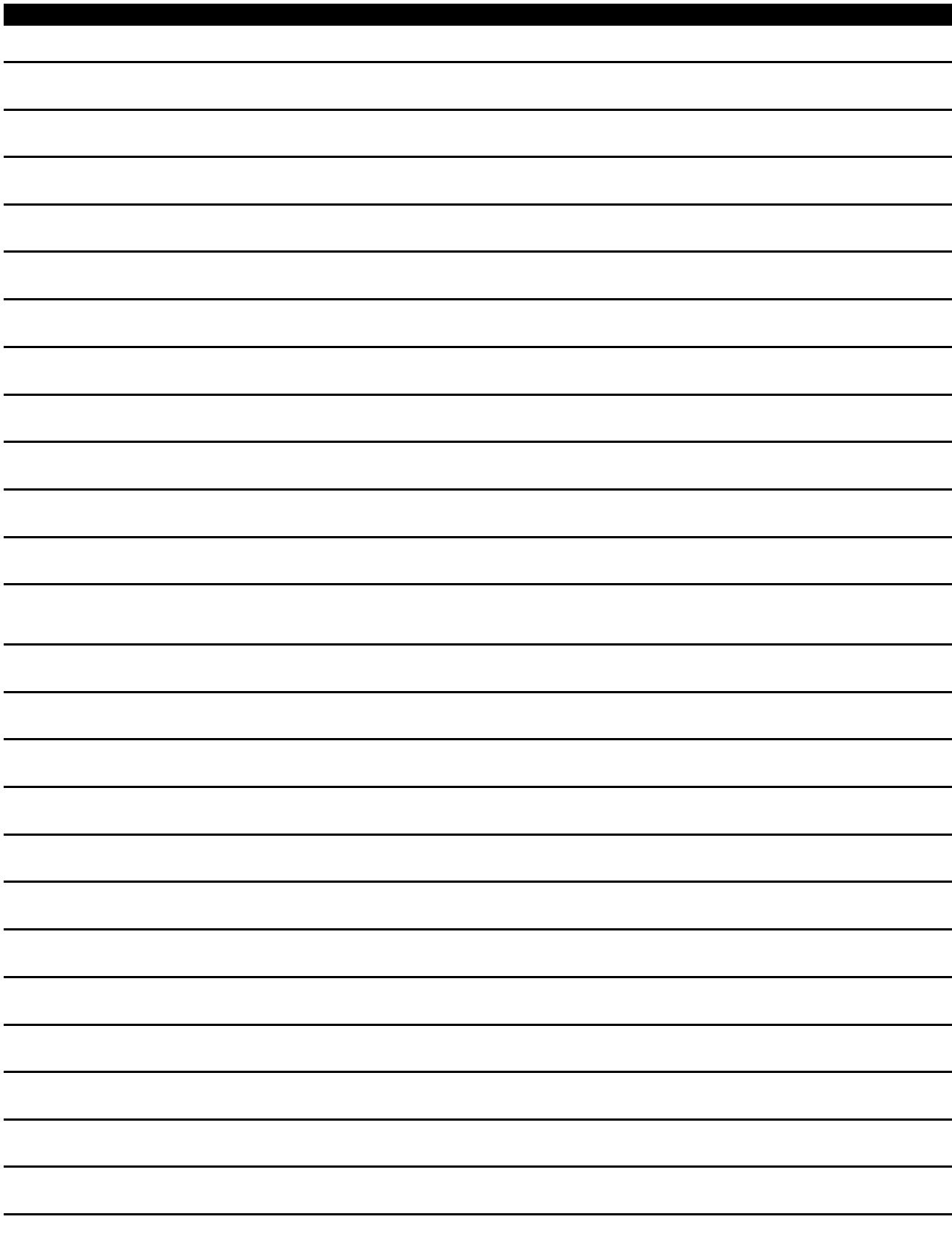
SELF TEST QUESTIONS

These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.

1. Describe briefly the scope of service tax in India.
2. Define the following:
 - (a) Service;
 - (b) Service tax.
3. Describe briefly the mechanism in administering service tax in India.
4. Explain in brief the steps for calculation of service tax under the new regime.

SUGGESTED READINGS

1. Taxation of Services – An Education Guide dated 20.06.2012
2. Service Tax Manual: *Taxmann*
2. *Dr. V.K. Singhania*: Students Guide to Income-tax; Taxmann Publications Pvt. Ltd., New Delhi.
3. *Girish Ahuja and Ravi Gupta*: Systematic Approach to Income-tax and Sales-tax; Bharat Law House, New Delhi.



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Lesson 10

Procedural Aspects and Adjudication under Service Tax

LESSON OUTLINE

- Registration Charge of Service tax
- Service Tax Registration of Special Category of Persons
- Payment of service tax
- Incidence to pay Service Tax
- Point of Taxation Rules, 2011
- Adjustment of Service Tax
- Interest on delayed payment of service tax u/s 75
- Records to be maintained
- E-filing of Service Tax Returns
- Cenvat Credit Rules, 2004
- Penalties and Prosecution
- Waiver or reduction of penalty
- Abatement in Service Tax
- Appeals
- Revision
- Advance Ruling
- Settlement Commission
- Audit Under Section 72A
- Role of Company Secretary
- Lesson Round Up
- Self Test Questions

LEARNING OBJECTIVES

This chapter covers the procedural as well substantive provisions relating to levy, collection and payment of service tax and relevant CENVAT Credit Rules 2004. It also covers the registration aspects, filing aspects including e-filing, appeal matters including appeal before Appellate Tribunal. The new regime of service tax i.e. levy of service tax on negative list approach have been discussed in the previous lesson.

At the end of this lesson, you will learn :

- What is the basis of charge for service tax?
- What are the circumstances under which service tax is paid by the receiver of services?
- When the liability for payment of service tax arises?
- What is the registration procedure for service provider?
- How to file service tax return?
- What are the Penal provisions for payment/non-payment of service tax?
- Adjudication procedures
- Provisions pertaining to advance ruling, Settlement Commission
- Audit under section 72A
- What is role of Company Secretaries?

CBEC has rolled-out a new centralized, web-based and workflow-based software application called Automation of Central Excise and Service Tax (ACES) for on-line filing/ uploading of documents and other activities under Central Excise and Service Tax.

A Certified Facilitation Centre (CFC) under ACES project is a facility, other than the physical front offices or Facilitation Centres of CBEC, which may be set-up and operated by a Company Secretary in practice to whom a certificate is issued under the ACES project, where the assessees of Central Excise and Service Tax can avail the facility to file their returns and other documents electronically on payment of specified fees.

REGISTRATION

Section 69 of the Finance Act, 1994 specifies the persons who are required to get themselves registered under this Act. Every person liable to pay service tax to get registered with designated Superintendent of Central Excise.

An application for registration is required to be made to the Superintendent of Central Excise in Form ST-1. This is to be made within a period of thirty days from the date on which the service tax is leviable on him and where a person commences the business of providing a taxable service after such service has been levied, he shall make an application for registration within a period of thirty days from the date of such commencement.

As stated earlier, a person can become liable to pay tax both as service provider as well as service receiver. Therefore, when a service receiver is liable to pay service tax he is also required to get himself registered.

Procedure for Registration

With effect from 1st June 2010 vide notification no.20-21/2010 a person shall make an online application for registration. Online registrations have been made mandatory for all the assessees. Assessee has to register via online portal of Automation of Central Excise and Service Tax (ACES) or can utilise the services Certified Facilitation Centres (CFCs) set up by Company Secretaries in practice under the (ACES) project of Central Board of Excise and Custom.

Assessee has to fill Form ST-1 for registration and thereafter submit the following documents as specified in Order No.2/2011 dated 13-12-2011:

- Copy of Permanent Account number (PAN);
- Proof of residence
- Constitution of applicant other than individuals at the time of filing an application for registration.
- Power of attorney in respect of authorized person.

Registration where the services are provided or received from more than one premises and having centralised accounting system in one or more premises:

Where a person, liable for paying service tax on a taxable service

- (i) provides such service from more than one premises or offices; or
- (ii) receives such service in more than one premises or offices; or,
- (iii) is having more than one premises or offices, which are engaged in relation to such service in any other manner, making such person liable for paying service tax, and has centralised billing system or centralised accounting system in respect of such service, and such centralised billing or centralised accounting systems are located in one or more premises, he may, at his option, register such premises or offices from where centralised *billing or centralised accounting systems are located*.

The registration under this case shall be granted by the Commissioner of Central Excise in whose jurisdiction the premises or offices, from where centralised billing or accounting is done, are located.

Registration where the services are provided or received from more than one premises and not having centralized accounting system:

Where an assessee is providing a taxable service from more than one premises or offices, and does not have any centralized billing systems or centralized accounting systems, as the case may be, he shall make separate applications for registration in respect of each of such premises or offices to the jurisdictional Superintendent of Central Excise.

Single Registration for Multiple Services

Where an assessee is providing more than one taxable service, he may make a single application, mentioning therein all the taxable services provided by him, to the concerned Superintendent of Central Excise.

Issue of Registration Certificate

The Superintendent of Central excise is bound to grant a certificate of registration in Form ST-2 within 7 days of the date of receipt of the application or intimation for any change or additional information provided by the applicant. This certificate shall indicate the details of all the taxable services provided by the service provider. In case of transfer of business by the assessee to another person, the transferee is required to obtain a fresh Certificate of Registration.

Surrender of Certificate of Registration

The registered assessee who ceases to provide the taxable services for which he had been registered shall surrender his Certificate of Registration to the concerned Superintendent of Central Excise.

SERVICE TAX REGISTRATION OF SPECIAL CATEGORY OF PERSONS

Input Service Distributor

Service Tax (Registration of Special Category of Persons) Rules, 2005 have come into effect on 16th day of June, 2005.

Registration under these rules can be obtained by an input service distributor by making an application to the jurisdictional Superintendent of Central Excise in such form as specified by the Board within a period of thirty days of the commencement of business or the 16th day of June, 2005, whichever is later.

Small Scale Service Provider

A small scale service provider has been specified as any provider of taxable service whose aggregate value of taxable service in a financial year does not exceed a certain specified limit. A small scale service provider whose aggregate value of taxable service in a financial year exceeds nine lakh rupees shall make an application to the jurisdictional Superintendent of Central Excise in the prescribed form for registration within a period of thirty days of exceeding the aggregate value of taxable service of nine lakh rupees.

However, a small scale service provider are not liable to pay service tax till they cross the exemption limit of ₹10 lakhs during a Financial Year.

PAYMENT OF SERVICE TAX

As per Section 68(1), every person providing taxable services i.e. provider of taxable service is liable to pay service tax at the rate specified in section 66B of the Finance Act, 1994 in such manner and within such period as may be prescribed.

Section 68(2), provides that in respect of the taxable services notified by the Central Government the service tax thereon shall be paid by such person as may be prescribed. Notification No. 30/2012 dated 20th June 2012 provides for the services where service tax shall be paid by service receiver or in some case by both i.e. service receiver and service provider. The mechanism under which liability for payment of service tax is

on the service receiver is known as **reverse charge**. Under this charge service receiver has to register himself under service tax. Further service receiver cannot claim general exemption limit of ₹ 10 Lakhs and he is liable to pay service tax even on small amount.

Below is the list of services covered under Reverse charge mechanism along with the share of service provider and share of service recipient on which they are required to pay service tax.

<i>Sl.No.</i>	<i>Description of a Service</i>	<i>Percentage of service tax payable by the person providing service</i>	<i>Percentage of service tax payable by the person receiving the service</i>
1	Services provided or agreed to be provided by an insurance agent to any person carrying on insurance business	Nil	100%
2	Services provided or agreed to be provided by a goods transport agency in respect of transportation of goods by road	Nil	100%
3	Services provided or agreed to be provided by way of sponsorship	Nil	100%
4	Services provided or agreed to be provided by an arbitral tribunal	Nil	100%
5	Services provided or agreed to be provided by individual advocate or a firm of advocates by way of legal services	Nil	100%
6	Services provided or agreed to be provided by way of support service by Government or local authority excluding renting of immovable property and services specified in section 66D(a) (i), (ii) & (iii)	Nil	100%
7	(a) In respect of services provided or agreed to be provided by way of renting or hiring any motor vehicle designed to carry passenger on abated value to any person who is not in the similar line of business.	Nil	100%
	(b) In respect of services provided or agreed to be provided by way of renting or hiring any motor vehicle designed to carry passenger on non abated value any person who is not in the similar line of business.	60%	40 %
8.	Services provided or agreed to be provided by way of supply of manpower for any purpose including security services	25%	75 %
9.	Services provided or agreed to be provided by way of works contract	50%	50%

10.	Any taxable services provided or agreed to be provided by any person who is located in a non-taxable territory and received by any person located in the taxable territory	Nil	100%
11.	Services provided or agreed to be provided by a director of a company to the said company	Nil	100%

INCIDENCE TO PAY SERVICE TAX

With effect from 1st July 2011, the liability to pay service tax was shifted from receipt basis to accrual basis with the introduction of Point of Taxation (POT) Rules, 2011. As per rule 3 of POT rules the liability to pay service tax shall arise upon issuance of invoice or receipt of payment whichever is earlier.

Proviso to Rule 6 of Service Tax Rules, 1994 has provided that in case of the individuals and partnership firms having an aggregate value of taxable services provided from one or more premises of ₹ 50 lakhs or less in the previous financial year, shall have the option to pay service tax upon receipt basis upto ₹ 50 lakhs in the current financial year.

The basic purpose for introduction of Point of Taxation Rules, 2011 is to bring clarity and certainty in matter of levy and collection of service tax in situations of:

- Change of rate of service tax
- Imposition of service tax on new services
- Continuous supply of services

Moreover, POT rules, 2011 have been introduced to bring synchronization between service tax and other taxes like Excise Duty and VAT which work on accrual basis and this is a step towards implementation of GST.

POT rules, 2011 were issued by the Central Government vide Notification No. 18/2011- ST dated 1st March, 2011 w.e.f. 1st April 2011. However, these rules were made effective w.e.f. 1st July 2011 vide Notification No.25/2011-ST dated 31st March 2011. Now, let us discuss the provisions of these rules:

Point of taxation means the point in time when a service shall be provided or deemed to have been provided. This Point of time will determine rate of service tax and due date of payment of service tax.

As per rule 2A of POT Rules, “Date of payment” shall be the earlier of the dates on which the payment is entered in the books of accounts or is credited to the bank account of the person liable to pay tax:

Provided that —

- (A) the date of payment shall be the date of credit in the bank account when—
 - (i) there is a change in effective rate of tax or when a service is taxed for the first time during the period between such entry in books of accounts and its credit in the bank account; and
 - (ii) the credit in the bank account is after four working days from the date when there is change in effective rate of tax or a service is taxed for the first time; and
 - (iii) the payment is made by way of an instrument which is credited to a bank account,
- (B) if any rule requires determination of the time or date of payment received, the expression “date of

payment" shall be construed to mean such date on which the payment is received".

As per Rule 3 of Point of Taxation Rules, Point of taxation shall be;

- (a) the time when the invoice for service provided or to be provided is issued or
- (b) in case where payment is received before the issue of invoice then the time when such payment is received or
- (c) where advance is received by the service provider the time of receipt of such advance.

Rule 4A of the Service Tax Rules, 1994, provides that every person providing taxable service shall issue invoice within 30 days of completion of service or receipt of payment of service whichever is earlier.

Further proviso to Rule 3 of POT Rules, provides that where the invoice is not issued within 30 days of completion of service than the point of taxation shall the date of completion of such service.

Examples:

S. No.	Date of Completion of service	Date of Invoice	Date on which payment is received	Point of taxation	Remarks
1	April 10, 2012	April 20, 2012	April 30, 2012	April 20, 2012	Invoice is issued within 30 days and before payment
2	April 10, 2012	May 26, 2012	April 30, 2012	April 10, 2012	Invoice not issued within 30 days and payment received after completion of service
3	April 10, 2012	April 20, 2012	April 15, 2012	April 15, 2012	Invoice is issued within 30 days and payment received before issue of invoice
4	April 10, 2012	May 26, 2012	April 5, 2012 (Part) and April 25, 2012 (remaining)	April 5, 2012 and April 10, 2012 for remaining	Advance received in part before completion of service and invoice not issued within 30 days of completion of service.

Continuous Supply of Service

"Continuous supply of service" means any service provided or agreed to be provided continuously or on recurrent basis, under a contract, for a period exceeding three months with the obligation for payment periodically or from time to time. Further, Central Government may notify provision of a particular service to be considered as continuous supply of service.

The following services have been notified vide Notification No. 28/2011 as continuous supply of service irrespective of period for which they are provided or to be provided;

- Telecommunication service
- Commercial or Industrial Construction Service
- Construction of Residential Complex
- Internet Communication
- Works contract services

As per Rule 3, in case of continuous supply of service, the point of taxation shall be the date of completion of the events as specified in the contract or time when invoice for the service provided or to be provided is issued or the date on which payment is received whichever is earlier. Where any advance is received by the service provider the point of taxation shall be date of receipt of each such advance. Further, where the invoice is not issued within 30 days of completion of such event then point of taxation shall be the date of completion of such event.

Point of Taxation in case of change in effective rate of tax (Rule 4)

Notwithstanding anything contained in rule 3, the point of taxation in cases where there is a change in effective rate of tax in respect of a service, shall be determined in the following manner, namely:-

- (a) in case a taxable service has been provided before the change in effective rate of tax,-
 - (i) where the invoice for the same has been issued and the payment received after the change in effective rate of tax, the point of taxation shall be date of payment or issuing of invoice, whichever is earlier; or
 - (ii) where the invoice has also been issued prior to change in effective rate of tax but the payment is received after the change in effective rate of tax, the point of taxation shall be the date of issuing of invoice; or
 - (iii) where the payment is also received before the change in effective rate of tax, but the invoice for the same has been issued after the change in effective rate of tax, the point of taxation shall be the date of payment;
- (b) in case a taxable service has been provided after the change in effective rate of tax,-
 - (i) where the payment for the invoice is also made after the change in effective rate of tax but the invoice has been issued prior to the change in effective rate of tax, the point of taxation shall be the date of payment; or
 - (ii) where the invoice has been issued and the payment for the invoice received before the change in effective rate of tax, the point of taxation shall be the date of receipt of payment or date of issuance of invoice, whichever is earlier; or
 - (iii) where the invoice has also been raised after the change in effective rate of tax but the payment has been received before the change in effective rate of tax , the point of taxation shall be date of issuing of invoice.

“Change in effective rate of tax” shall include a change in the portion of value on which tax is payable in terms of a notification issued in the Official Gazette under the provisions of the Act, or rules made thereunder.

Point of Taxation where Service is Taxed First Time (Rule 5)

Where a service is taxed for the first time, then, –

- (a) no tax shall be payable to the extent the invoice has been issued and the payment received against such invoice before such service became taxable;
- (b) no tax shall be payable if the payment has been received before the service becomes taxable and invoice has been issued within fourteen days of the date when the service is taxed for the first time.

Point of Taxation in case of Specified Services or Persons (Rule 7)

The point of taxation in respect of the persons required to pay tax as recipients of service under the rules made in this regard in respect of services notified under sub-section (2) of section 68 of the Act, shall be the date on which payment is made.

Provided that, where the payment is not made within a period of six months of the date of invoice, the point of taxation shall be determined as if this rule does not exist.

Provided further that in case of “associated enterprises”, where the person providing the service is located outside India, the point of taxation shall be the date of debit in the books of account of the person receiving the service or date of making the payment whichever is earlier.

Determination of Point of Taxation in case of intangibles (Rules 8)

In respect of royalties and payments pertaining to copyrights, trademarks, designs or patents, where the whole amount of the consideration for the provision of service is not ascertainable at the time when service was performed, and subsequently the use or the benefit of these services by a person other than the provider gives rise to any payment of consideration, the service shall be treated as having been provided each time;

- when a payment in respect of such use or the benefit is received by the provider in respect thereof, or
- an invoice is issued by the provider, whichever is earlier.

Determination of Point of Taxation based on best judgement (Rule 8A)

Where the point of taxation cannot be determined as per these rules as the date of invoice or the date of payment or both are not available, the Central Excise officer, may, require the concerned person to produce such accounts, documents or other evidence as he may deem necessary and after taking into account such material and the effective rate of tax prevalent at different points of time, shall, by an order in writing, after giving an opportunity of being heard, determine the point of taxation to the best of his judgment.

DUE DATE FOR PAYMENT OF SERVICE TAX

Rule 6(1) of the Service Tax Rules, 1994 specifies the time period for payment of service tax.

For individuals or proprietors or partnership firms:

The service tax shall be paid to the credit of the Central Government **by the 5th of the month immediately following the respective quarter** in which service is deemed to have been provided as per POT Rules made in this regard.

Where payment is made through internet banking, such e-payment can be made **by 6th of the month immediately following the respective quarter**.

However, for the quarter ending 31st March, the due date of payment of service tax shall be 31st March.

As stated earlier, individuals and partnership firms whose aggregate value of taxable services provided from one or more premises is fifty lakh rupees or less in the previous financial year, the service provider shall have option to pay the service tax on receipt basis by the due dates upto ₹50 lakhs in the current financial year.

For others

The service tax shall be paid to the credit of the Central Government by the 5th of the month immediately

following the calendar month in which service is deemed to have been provided.

Mandatory e-payment of service tax

Under proviso to Rule 6(2), e-payment of service tax is mandatory for the assessee, who has paid service tax of rupees one lakh (cash plus Cenvat credit) and above in the preceding financial year shall be deposit the service tax liable to be paid by him electronically, through internet banking.

Further, notwithstanding the time of receipt of payment towards the value of services, no service tax is payable for the part or whole of the value of services, which is attributable to services provided during the period when such services were not taxable.

Deposit of Service Tax

The assessee shall deposit the service tax liable to be paid by him with the bank designated by the Central Board of Excise and Customs in Form GAR – 7 challan.

Interest on Delayed Payment of Service Tax under Section 75

Every person, liable to pay the tax in accordance with the provisions of section 68 or rules made thereunder, who fails to credit the tax or any part thereof to the account of the Central Government within the period prescribed, shall pay simple interest at such rate not below 10% and not exceeding 36% p.a.

However where the service provider whose taxable services does not exceed ₹60 lakhs during any of the financial years covered by the notice or during the last financial year the rate of interest shall be reduced by 3% p.a.

ADJUSTMENT OF SERVICE TAX

(1) Adjustment of excess service tax paid on the services which are not so provided

Where an assessee has issued an invoice, or received any payment, against a service to be provided which is not so provided by him either wholly or partially for any reason, or where the amount of invoice is renegotiated due to deficient provision of service, or any terms contained in a contract the assessee may take the credit of such excess service tax paid by him, if the assessee,

- (a) has refunded the payment or part thereof, so received along with the service tax payable thereon for the service to be provided by him to the person from whom it was received;
- (b) has issued a credit note for the value of the service tax not so provided to the person to whom such an invoice had been issued.

(2) Adjustment of excess service tax paid in other cases

Where an assessee has paid to the credit of Central Government any amount in excess of the amount required to be paid towards service tax liability for a month or quarter, the assessee may adjust such excess amount paid by him against his service tax liability for the succeeding month or quarter.

The adjustment of excess amount paid, shall be subject to the conditions that the excess amount is paid on account of reasons not involving interpretation of law, taxability, valuation or applicability of any exemption notification.

VALUATION OF TAXABLE SERVICES

Section 67 provides for the method of valuation of taxable services i.e. the value on which service provider is

required to discharge service tax. As per section 67, the valuation of taxable service shall be determined under the following two situations:

- Service tax is separately charged in the bill
- Bill value is inclusive of service tax

Where the service tax is separately charged in the bill:

- (i) in a case where the provision of service is for a consideration in money, be the gross amount charged by the service provider for such service provided or to be provided by him;
- (ii) in a case where the provision of service is for a consideration not wholly or partly consisting of money, be such amount in money, with the addition of service tax charged, is equivalent to the consideration;
- (iii) in a case where the provision of service is for a consideration which is not ascertainable, be the amount as may be determined in the prescribed manner.

Where the bill is inclusive of service tax:

Where the gross amount charged by a service provider, for the service provided or to be provided is inclusive of service tax payable, the value of such taxable service shall be such amount as, with the addition of tax payable, is equal to the gross amount charged. In this case, value of taxable services shall be calculated as follows:

$$\text{Value of taxable Services} = \frac{\text{Gross Amount} \times 100}{100 + \text{Applicable rate of service tax}}$$

Example:

Pawan rendered a taxable service to a client on 25-08-2012. A bill of ₹ 40,000 was raised on 29-08-2012; ₹15,000 was received from the client on 1-10-2012 and the balance on 23-10-2012.

- (a) If service tax was separately charged in the bill, what is the value of taxable services and service tax payable?
- (b) No Service tax was separately charged in the invoice
 - Is Pawan liable to pay service tax, even though the same has not been charged by him?
 - In case, he is liable, what is the value of taxable services and service tax payable?

Solution

The bill is raised on 29-08-2012 but the payment is received in October 2012. As per Point of Taxation Rules, service tax shall be payable on or before 05-09-2012 or 06-09-2012 and not in October when payment is received.

Therefore, in this case service tax shall be payable as;

- (a) Value of taxable service is ₹ 40,000, therefore service tax shall be payable @12% Plus Education @2% and SHEC@1%.

$$\text{Service tax} = ₹40,000 \times 12.36\% = ₹ 4944/-$$

- (b) Pawan is liable to pay service tax even though the tax has not been collected by him. The service tax payable shall be;

$$= 40,000 \times 12.36/112.36 = ₹ 4400/-$$

ABATEMENT IN SERVICE TAX

Abatement in Service Tax is a major relief to certain kinds of services which are chargeable to service tax. Finance Act 1994 provides that for determining value of service tax on which service tax is to be charged abatement in value determination is allowed.

Abatement under service tax laws means that for certain services, a specified percentage of discount is allowed from the gross amount collected for rendering the services subject to the conditions that CENVAT Credit has not been availed by the service provider.

Notification No. 26/2012- ST dated 20/06/2012 provides the list of services on which abatement is allowed. It also provides for the percentage on which service tax is payable under the scheme of abatement. The concept of abatement may be understood with the help of this example;

As per notification no. 26/2012, railway is required to charge service tax only on 30% value of the Taxable services. Thereby by virtue of this provision, if railways receive an amount of ₹ 50 Lakhs against the services, it needs to pay service tax only on ₹ 15 Lakhs i.e. 30% value of ₹ 50 Lakhs.

RECORDS TO BE MAINTAINED

Every assessee shall furnish to the Superintendent of Central Excise at the time of filing of return for the first time or the 31st day of January, 2008, whichever is later, a list in duplicate, of-

- (i) all the records prepared or maintained by the assessee for accounting of transactions in regard to,-
 - (a) providing of any service,
 - (b) receipt or procurement of input services and payment for such input services;
 - (c) receipt, purchase, manufacture, storage, sale, or delivery, as the case may be, in regard of inputs and capital goods;
 - (d) other activities, such as manufacture and sale of goods, if any.
- (ii) all other financial records maintained by him in the normal course of business;

All such records shall be preserved at least for a period of five years immediately after the financial year to which such records pertain.

The records including computerised data, as maintained by an assessee in accordance with the various laws in force from time to time shall be acceptable.

RETURNS UNDER SERVICE TAX

Rule 7 of the Service Tax Rules, 1994 return under Service Tax is required to be filed by every assessee on half yearly basis in Form ST-3 or Form ST-3A, as the case may be, along with a copy of the Form TR-6/GAR-7, in triplicate for the months covered in the half-yearly return.

Every assessee shall submit the half yearly return by the 25th of the month following the particular half-year. Every assessee is required to file return electronically.

Vide Notification No. 43/2011 dt. 25th August 2011, every Assessee shall submit a half yearly return electronically. Assessee can file service tax return online at registering at <https://www.aces.gov.in>.

With effect from 1st October, 2011, every assessee is required to file half yearly return electronically.

Revision of Returns

As per Rule 7B, an assessee may submit a revised return, in Form ST-3, in triplicate, to correct a mistake or omission, within a period of ninety days from the date of submission of the return under rule 7.

Penalty for not filing and late Filing of Return

If return of service tax is not filed within the prescribed period penalty is leviable under section 77(2) which can be upto ₹10,000.

Rule 7C of Service Tax Rules, 1994 provides for penalty for delay in filing of service tax return. Accordingly late fee is payable as follows:

Delay upto 15 days	₹ 500/-
Delay beyond 15 days and upto 30 days	₹ 1,000/-
Delay beyond 30 days	₹1,000 + ₹ 100/- per day subject to a maximum of ₹ 20,000/ [the penalty prescribed in section 70(1)]

Penalty for late filing of return is specifically prescribed in Rule 7C subject to section 70 therefore if late fee is paid then no penalty prescribed under section 77(2) shall be leviable.

PENALTIES AND PROSECUTION

Various penalties have been provided under the Act. Section 83A empowers Central Excise Officer to adjudicate penalty within such powers as may be conferred by CBEC, by issuing a notification.

(A) PENALTY FOR FAILURE TO PAY SERVICE TAX [SECTION 76]

Any person who fails to pay service tax, shall pay, in addition to such tax and the interest on that tax amount in accordance with the provisions of section 75, a penalty which shall not be less than;

- one hundred rupees for every day during which such failure continues; or
- at the rate of one per cent. of such tax, per month, whichever is higher, starting with the first day after the due date till the date of actual payment of the outstanding amount of service tax.

Provided that the total amount of the penalty payable in terms of this section shall not exceed 50% of the service tax payable.

Example

X, an assessee, fails to pay service tax of ₹10 lakhs payable by 5th March. X pays the amount on 15th March. The default has continued for 10 days. The penalty payable by X is computed as follows:-

- 1% of the amount of default for 10 days = $1 \times 10,00,000 \times 10/31 = ₹3,225.80$ or
 - Penalty calculated @ ₹100 per day for 10 days = ₹1,000
- Penalty liable to be paid is ₹ 3,226.00.

(B) PENALTY FOR CONTRAVENTION OF RULES AND PROVISIONS OF ACT FOR WHICH NO PENALTY IS SPECIFIED ELSEWHERE [SECTION 77]

- (a) Any person who is liable to pay service tax, or required to take registration, fails to take registration shall be liable to pay a penalty which may extend to **ten thousand rupees**.

- (b) Any person who fails to keep, maintain or retain books of account and other documents shall be liable to a penalty which may extend to **ten thousand rupees**.
- (c) Any person who fails to —
 - (i) furnish information called by an
 - (ii) produce documents called for by a Central Excise Officer
 - (iii) appear before the Central Excise Officer, when issued with a summon for appearance to give evidence or to produce a document in an inquiry, shall be liable to a penalty which may extend to;
 - ten thousand rupees or
 - two hundred rupees for every day during which such failure continues, whichever is higher, starting with the first day after the due date, till the date of actual compliance.
- (d) Any person who is required to pay tax electronically, through internet banking, fails to pay the tax electronically, shall be liable to a penalty which may extend to **ten thousand rupees**.
- (e) Any person who issues invoice with incorrect or incomplete details or fails to account for an invoice in his books of account, shall be liable to a penalty which may extend to **ten thousand rupees**.
- (f) Any person, who contravenes any of the provisions or any rules for which no penalty is separately provided, shall be liable to a penalty which may extend to **Ten thousand rupees**

(C) PENALTY FOR SUPPRESSING VALUE OF TAXABLE SERVICE [SECTION 78]

Where any service tax has not been levied or paid or has been short-levied or short-paid or erroneously refunded, by reason of

- (a) fraud; or
- (b) collusion; or
- (c) wilful mis-statement; or
- (d) suppression of facts; or
- (e) contravention of any of the provisions or of the rules with intent to evade payment of service tax the person shall be liable to pay service tax or erroneous refund, and

shall be liable to pay a penalty, in addition to such service tax and interest which shall equal to the amount of service tax so not levied or short-paid or erroneously refunded.

However the amount of penalty shall be reduced to:

- (a) 50% where true and complete details of the transactions are available in the specified records.
- (b) 25% where true and complete details of the transactions are available in the specified records and the amount of service tax, interest and penalty has been paid within 30 days.

In case of service providers whose taxable value of service tax does not exceed ₹ 60 lakhs, the period of 30 days shall be extended to 90 days.

Section 78 provides that if penalty is applicable under this section, provisions section 76 shall be apply. Thus, the assessee is relieved from effects of dual penalty.

(D) PENALTY FOR OFFENCES BY DIRECTOR, ETC., OF COMPANY [Section 78A]

Where a company has committed any of the following contraventions, namely:—

- (a) evasion of service tax; or
- (b) issuance of invoice, bill or, as the case may be, a challan without provision of taxable service in violation of the rules made under the provisions of this Chapter; or
- (c) availment and utilisation of credit of taxes or duty without actual receipt of taxable service or excisable goods either fully or partially in violation of the rules made under the provisions of this Chapter; or
- (d) failure to pay any amount collected as service tax to the credit of the Central Government beyond a period of six months from the date on which such payment becomes due, then
 - any director, manager, secretary or other officer of such company,
 - who at the time of such contravention was in charge of, and was responsible to,
 - the company for the conduct of business of such company and was knowingly concerned with such contravention,

shall be liable to a penalty which may extend to one lakh rupees.

WAIVER OR REDUCTION OF PENALTY

As per Section 80, penalty under Sections 76, 77 or first proviso to section 78 (1) can be waived if assessee proves that he had reasonable cause for the failure.

PROSECUTION

Section 89 was inserted by Finance Act, 2011 which provides for offences which can lead to prosecution. The prosecution was introduced in service tax to promote self compliance among the assessee. Further, sections 9A, 9AA, 9B, 9E and 34A of the Central Excise Act, 1944 have been made applicable service tax. These provisions together constitute the provisions relating to prosecution of offences.

CENVAT CREDIT RULES, 2004

The CENVAT Credit Rules, 2004 have replaced the existing Cenvat Credit Rules, 2002 and Service tax Credit Rules, 2002 with effect from 10th September 2004. The new Rules integrated services with goods. With the introduction of these rules, inter sectoral credit is allowed to be taken. Service tax paid on input service is allowed to be used for duty payable on final products removed. Similarly, excise duty paid on inputs is allowed to be used for paying service tax on output service.

Example:

Duty paid on raw plastic for the manufacture of plastic furniture is ₹ 20,000 and service tax paid on transportation i.e. Goods Transport Agency of raw plastic of ₹ 10,000. The duty payable on the finished goods (plastic furniture) is ₹ 35,000 while paying the duty on plastic furniture; the manufacturer is allowed to deduct the amount already paid as excise duty and service tax (Input tax) on raw plastic. Thus, the net duty payable will be ₹ 5,000 only. Technically speaking, the manufacturer availed the cenvat credit to the extent of ₹ 30,000 that he paid on inputs and input service for manufacturing of plastic furniture.

Note: The provisions of CENVAT Credit Rules are covered in detail at Lesson No. 5 Part V of this Study.

ADVANCE RULING (SECTION 96A TO 96-I)

“Advance ruling” means the determination, by the Authority, of a question of law or fact specified in the application regarding the liability to pay service tax in relation to a service proposed to be provided, by the applicant.

“Applicant” means –

- (i) (a) a non-resident setting up a joint venture in India in collaboration with a non-resident or a resident; or
- (b) a resident setting up a joint venture in India in collaboration with a non-resident; or
- (c) a wholly owned subsidiary Indian company, of which the holding company is a foreign company, who or which, as the case may be, proposes to undertake any business activity in India.
- (ii) a joint venture in India.
- (iii) a resident falling within any such class or category of persons, as the Central Government may, by notification in the Official Gazette, specify in this behalf.

Authority for Advance Ruling: Authority for Advance Ruling under Service Tax shall be the same as constituted under Section 28F(2A) of Customs Act, 1962.

APPLICATION FOR ADVANCE RULING

An applicant desirous of obtaining an advance ruling under this Chapter may make an application in such form and in such manner as may be prescribed, stating the question on which the advance ruling is sought.

The question on which the advance ruling is sought shall be in respect of,-

- (a) classification of any service as a taxable service under Chapter V;
- (b) the valuation of taxable services for charging service tax;
- (c) the principles to be adopted for the purposes of determination of value of the taxable service under the provisions of Chapter V;
- (d) applicability of notifications issued under Chapter V;
- (e) admissibility of credit of service tax;
- (f) determination of the liability to pay service tax on a taxable service under the provisions of Chapter V.

The application shall be made in quadruplicate and be accompanied by a fee of two thousand five hundred rupees.

An applicant may withdraw an application within thirty days from the date of the application.

PROCEDURE ON RECEIPT OF APPLICATION

The authority is required to give its ruling within 90 days of the receipt of valid application.

An application may be rejected by the prescribed authority if the question or subject matter of ruling sought in the application is such which is already pending before any assessing officer, Tribunal and court of law or such question already stands decided by any court or bench of Tribunal.

APPLICABILITY OF ADVANCE RULING

The advance ruling pronounced by the Authority shall be binding only-

- (a) on the applicant who had sought it;
- (b) on the Commissioner of Central Excise, and the Central Excise authorities subordinate to him, in respect of the applicant.

The advance ruling shall be binding unless there is a change in law or facts on the basis of which the advance ruling has been pronounced.

No proceeding before, or pronouncement of advance ruling by, the Authority shall be invalid on the ground merely of the existence of any vacancy or defect in the constitution of the Authority.

APPEALS

Appeal can be filed against adjudication order as per following provisions.

- If adjudication order is passed by authority lower than Commissioner of Central Excise, first appeal will be with Commissioner (Appeals) under Section 85(1) within three months from date of receipt of order made before the 28th May 2012 (the date Finance Bill receives the assent of the president) of adjudicating authority. Further, the appeal shall be presented within two months from the date of receipt of order made on and after 28th May 2012.

Second and final appeal is with Appellate Tribunal (known as – Customs, Excise and Service Tax Appellate Tribunal – CESTAT) under Section 86(1). Appeal is required to be filed within three months of the date of receipt of the order.

APPEALS TO THE COMMISSIONER OF CENTRAL EXCISE (APPEALS) [SECTION 85]

- Any person aggrieved by any decision or order passed by an adjudicating authority subordinate to the Commissioner of Central Excise may appeal to the Commissioner of Central Excise (Appeals).
- Every appeal shall be in the prescribed form and shall be verified in the prescribed manner.
- An appeal shall be presented within three months from date of receipt of order made before the 28th May 2012 (the date Finance Bill receives the assent of the president) of adjudicating authority. Further, the appeal shall be presented within two months from the date of receipt of order made on and after 28th May 2012.

Condonation of delay

- The Commissioner of Central Excise (Appeals) may, if he is satisfied that the appellant was prevented by sufficient cause from presenting the appeal within the aforesaid period of three months, allow it to be presented within a further period of three months if the order made before 28th May 2012. If order made on and after 28th May 2012 then the delay may be condoned for a further period of one month.
- The Commissioner of Central Excise (Appeals) shall hear and determine the appeals and, pass such orders as he thinks fit and such orders may include an order enhancing the service tax, interest or penalty

Principle of Natural Justice

- an order enhancing the service tax, interest or penalty shall not be made unless the person affected thereby has been given a reasonable opportunity of showing cause against such enhancement.

APPEAL TO TRIBUNAL (SECTION 86)

Any assessee aggrieved by an order passed by a Commissioner of Central Excise under section 73 or section 83A, or an order passed by a Commissioner of Central Excise (Appeals) under section 85, may appeal to the Appellate Tribunal against such order.

The Committee of Chief Commissioners of Central Excise may, if it objects to any order passed by the Commissioner of Central Excise under section 73 or section 83A or section 84, or by the Commissioner of Central Excise(Appeals) under section 85 direct the Commissioner of Central Excise to appeal to the Appellate Tribunal against the order.

Every appeal shall be filed within four months of the date on which the order sought to be appealed against is received by the assessee, the Committee of Chief Commissioners.

The Commissioner of Central Excise or any Central Excise Officer subordinate to him or the assessee, notwithstanding that he may not have appealed against such order within forty-five days of the receipt of the notice, file a memorandum of cross-objections, verified in the prescribed manner.

The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period if it is satisfied that there was sufficient cause for not presenting it within that period.

Every application made before the Appellate Tribunal,

- (a) in an appeal for grant of stay or for rectification of mistake or for any other purpose; or
- (b) for restoration of an appeal or an application, shall be accompanied by a fee of five hundred rupees.

Provided that no such fee shall be payable in the case of an application filed by the Commissioner of Central Excise or Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise.

FURTHER APPEALS

Further appeals against order of Tribunal (CESTAT) lies with Supreme Court only in matters of valuation and classification. If there is substantial question of law (other than classification and valuation), appeal has to be filed with High Court.

SETTLEMENT COMMISSION

Vide Notification No. 16/2012-ST dated 29th May 2012, the provisions contained in sections 31, 32 and 32A to 32P of the Central Excise Act, 1944 (1 of 1944) made applicable to service tax vide section 83 of the Act, 1994. All these provisions pertaining to Settlement Commission are discussed in detail under lesson no. 7. Further, in addition to the provisions contained in Central Excise the Service Tax (Settlement of Cases) Rules, 2012 shall also need to go through.

Form and manner of Application

As per Rule 3(1) of the Service Tax (Settlement of cases) Rules, 2012 provides for form and manner of application. An application under sub-section (1) of section 32E of Excise Act, made applicable to service tax vide section 83 of the Act, shall be made in the Form SC(ST)-1.

The application referred to in rule 3(1), the verification contained therein and all relevant documents accompanying such application shall be signed,-

- (a) in the case of an individual, by the individual himself or where the individual is absent from India, by

the individual concerned or by some person duly authorised by him in this behalf; and where the individual is a minor or is mentally incapacitated from attending to his affairs, by his guardian or by any other person competent to act on his behalf;

- (b) in the case of a Hindu undivided family, by the *Karta* of such family and, where the *Karta* is absent from India or is mentally incapacitated from attending to his affairs, by the senior most adult member of the family available;
- (c) in the case of a company or local authority, by the principal officer thereof;
- (d) in the case of a firm, by any partner thereof, not being a minor;
- (e) in case of any other association, by any member of the association or the principal officer thereof; and
- (f) in the case of any other person, by that person or some person competent to act on his behalf.

Every application in the Form SC(ST)-1 shall be filed in quintuplicate and shall be accompanied by a fee of one thousand rupees.

The additional amount of service tax accepted by the applicant along with interest due thereon, shall be deposited by him in any of the authorised bank under TR-6, referred to in the Service Tax Rules, 1994 (hereinafter referred to as TR-6 Challan) in quintuplicate, or G.A.R.-7 and shall be disclosed by him in the Form [Rule 3(4)].

Disclosure of information in the application for settlement of cases:

The Settlement Commission shall, while calling for a report from the Commissioner of Central Excise having jurisdiction or Commissioner of Service Tax having jurisdiction, under sub-section (3) of section 32F of Excise Act, made applicable to service tax vide section 83 of the Act, forward a copy of the application referred to in sub-rule (1) of rule 3 along with the annexure to the application and the statements and other documents accompanying such annexure (Rule 4).

Manner of provisional attachment of property

Where the Settlement Commission orders attachment of property under sub-section (1) of section 32G of Excise Act, made applicable to service tax vide section 83 of the Act, it shall send a copy of such order to the Commissioner of Central Excise or Commissioner of Service Tax having jurisdiction over the place in which the applicant owns any movable or immovable property or resides or carries on his business or has his bank account.

On receipt of the order, the Commissioner may authorise any officer subordinate to him and not below the rank of an Assistant Commissioner of Central Excise or Service Tax to take steps to attach such property of the applicant.

The officer authorised shall prepare an inventory of the property attached and specify in it, in the case of the immovable property, the description of such property sufficient to identify it and in case of the movable property, the place where such property is lodged or kept and shall hand over a copy of the same to the applicant or to the person from whose charge the property is attached.

The officer authorised shall send a copy of the inventory so prepared each to the Commissioner of Central Excise and the Settlement Commission.

Fee for copies of reports

Any person who makes an application under section 32J of Excise Act, made applicable to service tax vide

section 83 of the Act, for obtaining copies of reports made by any Central Excise Officer, shall pay a fee of five rupees per page of each report or part thereof.

SPECIAL AUDIT UNDER SECTION 72A

If the Commissioner of Central Excise, has reasons to believe that any person liable to pay service tax

- (i) has failed to declare or determine the value of a taxable service correctly; or
- (ii) has availed and utilised credit of duty or tax paid-
 - (a) which is not within the normal limits having regard to the nature of taxable service provided, the extent of capital goods used or the type of inputs or input services used, or any other relevant factors as he may deem appropriate; or
 - (b) by means of fraud, collusion, or any wilful misstatement or suppression of facts; or
- (iii) has operations spread out in multiple locations and it is not possible or practicable to obtain a true and complete picture of his accounts from the registered premises falling under the jurisdiction of the said Commissioner, he may direct such person to get his accounts audited by a chartered accountant or cost accountant nominated by him, to the extent and for the period as may be specified by the Commissioner.

The Chartered Accountant or Cost Accountant shall, within the period specified by the said Commissioner, submit a report duly signed and certified by him to the said Commissioner mentioning therein such other particulars as may be specified by him.

The Audit under this Section shall be carried out even if the accounts of a person have been audited under any other law for the time being in force.

The person liable to pay tax shall be given an opportunity of being heard in respect of any material gathered on the basis of the audit and proposed to be utilised in any proceedings.

ROLE OF COMPANY SECRETARIES

There is a great scope for Company Secretaries in Practice in the area of service tax. A Practicing Company Secretary can render several services under the Service Tax such as;

- Consultancy services: The company secretaries can provide expertise services to their clients by explaining and interpreting the provisions of the transformed and upcoming legislations. For Example, the taxability of services shifted from selective approach to negative approach.
- Compliance Services: The Company Secretaries can help the client or employers to comply with the following procedural requirement:
 - (a) Registration
 - (b) Payment of tax
 - (c) Maintenance of books and records
 - (d) Availment and utilization of Cenvat Credit
 - (e) Submissions of service tax returns.
- Certified Facilitation Centres (CFCs): Company Secretaries in Practice can set up CFCs under the Automation of Central Excise and Service Tax Project of CBEC to provide procedural compliance services to the assessees by charging fees.

LESSON ROUND UP

- Registration of service tax: Section 69 of the Finance Act, read with Rule 4 of the Service Tax Rules make provisions relating to registration. It is mandatory for every person liable to pay service tax to get registered with Superintendent of Central Excise. A person providing a taxable service is liable to pay service tax in terms of Section 68.
- An application for registration to the Superintendent of Central Excise can be made in form (ST-1). This is to be made within a period of thirty days from the date on which the service tax is leviable.
- Payment of service tax: With effect from 1st April 2011, Finance Act, 2011 introduced Point of Taxation (POT) Rules, 2011. These rules laid down the provisions relating to payment of service tax on accrual basis instead of receipt basis and specify the relevant date for determining rate of service tax. Point of taxation means the point in time when a service shall be deemed to have been provided. This Point of time will determine rate of service tax and due date of payment of service tax.
- Reverse charge- As per Section 68, every person providing taxable services i.e. provider of output service is liable to pay service tax. But in special cases service receiver is liable to pay service tax. This is known as reverse charge. Under this charge service receiver has to register himself under service tax. Further service receiver can not claim general exemption limit of 10 Lakhs rupees and he is liable to pay service tax even on small amount.
- Section 67 provides for the method of valuation of taxable services i.e. the value on which service provider is required to discharge service tax. As per section 67, the valuation of taxable service shall be determined under the following two situations:
 - Service tax is separately charged in the bill
 - Bill value is inclusive of service tax
- Abatement under service tax laws means that for certain services, a specified percentage of discount is allowed from the gross amount collected for rendering the services subject to the conditions that CENVAT Credit has not been availed by the service provider.
- Adjustment of Service tax: Where an assessee has paid to the credit of Central Government any amount in excess of the amount required to be paid towards service tax liability for a month or quarter, the assessee may adjust such excess amount paid by him against his service tax liability for the succeeding month or quarter.
- Maintenance of Accounts: Every assessee is required to furnish to the Superintendent of Central Excise at the time of filing his return for the first time, a list of all accounts maintained by him in relation to service tax including memoranda received from his branch offices.
- Filing of return: Rule 7 of the Service Tax Rules, 1994 return under Service Tax is required to be filed by every assessee on half yearly basis in Form ST-3 or Form ST-3A, as the case may be, along with a copy of the Form GAR -7, in triplicate for the months covered in the half-yearly return. Every assessee shall submit the half yearly return by the 25th of the month following the particular half-year.
- E-filing of return: With effect from 1st October, 2011, every assessee is required to file half yearly return electronically.
- Interest on late payment of service tax: Every person, liable to pay the tax in accordance with the provisions of section 68 or rules made thereunder, who fails to credit the tax or any part thereof to the account of the Central Government within the period prescribed, shall pay simple interest at such rate not below 10% and not exceeding 36% p.a.

- **Doctrine of unjust enrichment:** Since service tax is indirect tax, it is recoverable from customer. If you recover the amount from customer and again claim refund, you will get double benefit. Hence, provision of 'unjust enrichment' has been made in the law. As per the doctrine of unjust enrichment, refund will be granted to assessee only if assessee had not passed on the tax burden to your customer/client. It will be presumed that assessee has passed on the burden of service tax.
- **Penalties:** Various penalties have been provided under the Act. The penalties can be imposed by Central Excise Officers. There is no provision for prosecution under the Act.
- **Role of Company Secretaries:** The educational background, knowledge, training and exposure that a Company Secretary has, makes him a versatile professional capable of rendering a wide range of services to companies of all sizes, other commercial and industrial organizations, small scale units, firms etc.

SELF TEST QUESTIONS

These are meant for re-capitulation only. Answers to these questions are not to be submitted for evaluation.

1. What are the various provisions relating to payment of service tax? Explain.
2. What are the provisions regarding penalties under service tax in the following cases :
 - (a) Failure to take registration.
 - (b) Failure to keep books of account.
 - (c) Failure to produce accounts and documents.
3. "The value of any taxable service shall be the gross amount charged by the service provider for such service rendered by him". In the light of this statement, explain how the value of taxable service is determined.
4. Briefly state the provisions relating to the procedure of registration under the service tax.
5. What are the due dates for payment of service tax by different assessees ?
6. Indicate the amount of interest payable for late payment of service tax and the amount of penalty payable for late filing of return of service tax.
7. Explain the provisions regarding submission of return under service tax.
8. What is the basis of calculation of service tax payable? Explain the provisions governing valuation of taxable services.
9. "Service tax is generally payable by the service provider, but there are certain situations in which service receiver is liable to pay service tax." Explain.
10. Discuss 'advance ruling in service tax'.
11. Explain the provisions regarding service tax on Company Secretaries.

SUGGESTED READINGS

1. *Dr. V.K. Singhania* : Students Guide to Income-tax; Taxmann Publications Pvt. Ltd., New Delhi.
2. *Girish Ahuja and Ravi Gupta* : Systematic Approach to Income-tax and Sales-tax; Bharat Law House, New Delhi.
3. Service Tax Manual: *Taxmann*

Lesson 11

Goods and Service Tax- Concept and Developments

LESSON OUTLINE

- Introduction
- Meaning of GST
- Justification of GST
- GST Model
- Taxes subsumed under GST
- Rate structure under GST
- Constitution Amendment Bill
- Learning Objective
- Self Test Questions

LEARNING OBJECTIVES

Indian economy is getting more and more globalised. In recent times, a number of Free Trade Agreements (FTAs) have been signed, which will allow duty free imports into India or at very low duties. Hence, there is a need to have a nation-wide simple and transparent system of taxation to enable the Indian industry to compete not only internationally, but also in the domestic market. Integration of various Central and State taxes into a GST system would make it possible to give full credit for inputs taxes collected. GST, being a destination-based consumption tax based on VAT principle, would also greatly help in removing economic distortions caused by present complex tax structure and will help in development of a common national market.

Accordingly, a proposal to introduce a national level Goods and Services Tax (GST) by April 1, 2010 was first mooted by the then Finance Minister Shri P. Chidambaram in his Budget Speech for the financial year 2006-07. Since the proposal involved reform/ restructuring of not only indirect taxes levied by the Centre but also the States, the responsibility of preparing a Design and Road Map for the implementation of GST was assigned to the Empowered Committee of State Finance Ministers chaired by Dr. Asim K. Dasgupta, Finance Minister of West Bengal. Thereafter, certain developments had taken place in the sphere of GST.

At the end of this lesson the students will be well acquaint with

- Concept of GST
- Developments taken place from time to time
- Taxes subsumed under GST
- Rate Structure proposed under GST
- GST Model

Almost 140 countries have already implemented the GST. Most of the countries have a unified GST System. Brazil and Canada follow a dual system where GST is levied by both the Union and State Governments. France was the first country to introduce GST System in 1954.

INTRODUCTION

An announcement was made by Shri P. Chidambaram, the then Union Finance Minister in the Central Budget (2007-2008) to the effect that GST would be introduced from April 1, 2010. After this announcement, the Empowered Committee of State Finance Ministers decided to set up a Joint Working Group (May 10, 2007). This Joint Working Group, after intensive internal discussions as well as interaction with experts and representatives of Chambers of Commerce and Industry, submitted its report to the Empowered Committee (November 19, 2007). This report was then discussed in detail in the meeting of Empowered Committee (November 28, 2007). On the basis of this discussion and written observations of the States, certain modifications were made and a final version of the views of Empowered Committee at that stage was prepared and was sent to the Government of India (April 30, 2008). The comments of the Government of India were received on December 12, 2008 and were duly considered by the Empowered Committee (December 16, 2008). Based on inputs from GoI and States, The EC released its First Discussion Paper on Goods and Services Tax in India on the 10th of November, 2009 with the objective of generating a debate and obtaining inputs from all stakeholders.

A dual GST model for the country has been proposed by the EC. This dual GST model has been accepted by centre. Under this model GST have two components viz. the Central GST to be levied and collected by the Centre and the State GST to be levied and collected by the respective States. Central Excise duty, additional excise duty, Service Tax, and additional duty of customs (equivalent to excise), State VAT, entertainment tax, taxes on lotteries, betting and gambling and entry tax (not levied by local bodies) would be subsumed within GST.

In order to take the GST related work further, a Joint Working Group consisting of officers from Central as well as State Government was constituted. This was further trifurcated into three Sub-Working Groups to work separately on draft legislations required for GST, process/forms to be followed in GST regime and IT infrastructure development needed for smooth functioning of proposed GST. In addition, an Empowered Group for development of IT Systems required for Goods and Services Tax regime has been set up under the chairmanship of Dr. Nandan Nilekani.

Constitutional Amendment

The Constitution provides for delineation of power to tax between the Centre and States. While the Centre is empowered to tax services and goods upto the production stage, the States have the power to tax sale of goods. The States do not have the powers to levy a tax on supply of services while the Centre does not have power to levy tax on the sale of goods. Thus, the Constitution does not vest express power either in the Central or State Government to levy a tax on the 'supply of goods and services'. Moreover, the Constitution also does not empower the States to impose tax on imports. Therefore, it is essential to have Constitutional Amendments for empowering the Centre to levy tax on sale of goods and States for levy of service tax and tax on imports and other consequential issues.

Hence, The 115th Constitutional Amendment Bill, 2011 ("Bill") was tabled before the Parliament by the Finance Minister on March 22, 2011. The Bill proposes to amend the Constitution to empower the Union and States to frame laws for levying goods and service tax ("GST") on transactions involving supply of goods and services.

WHAT IS GOODS AND SERVICE TAX

GST is a tax on goods and services with comprehensive and continuous chain of set-off benefits from the

producer's point and service provider's point upto the retailer's level. It is essentially a tax only on value addition at each stage, and a supplier at each stage is permitted to set-off, through a tax credit mechanism, the GST paid on the purchase of goods and services as available for set-off on the GST to be paid on the supply of goods and services. The final consumer will thus bear only the GST charged by the last dealer in the supply chain, with set-off benefits at all the previous stages.

Illustration

Stage of supply chain	Purchase of Value	value addition	Value at which supply of goods and services output made to next stage	Rate of GST	GST on Input	Input tax credit	Net GST= GST on output-Input Tax credit
Manufacturer	100	30	130	10%	13	10	13–10 = 3
Whole seller	130	20	150	10%	15	13	15–13 = 2
Retailer	150	10	160	10%	16	15	16–15 = 1

‘GST’ has also been defined under Article 366 (Clause 12A) of Constitution Amendment Bill, 2011 to mean any tax on the supply of goods or services or both excluding supply of petroleum crude, high speed diesel, motor spirit, natural gas, aviation turbine fuel and alcoholic liquor for human consumption.

JUSTIFICATION OF GST

There was a burden of “tax on tax” in the pre-existing Central excise duty of the Government of India and sales tax system of the State Governments. The introduction of Central VAT (CENVAT) has removed the cascading burden of “tax on tax” to a good extent by providing a mechanism of “set off” for tax paid on inputs and services upto the stage of production, and has been an improvement over the pre-existing Central excise duty. Similarly, the introduction of VAT in the States has removed the cascading effect by giving set-off for tax paid on inputs as well as tax paid on previous purchases and has again been an improvement over the previous sales tax regime.

But both the CENVAT and the State VAT have certain incompleteness. The incompleteness in CENVAT is that it has yet not been extended to include chain of value addition in the distributive trade below the stage of production. It has also not included several Central taxes, such as Additional Excise Duties, Additional Customs Duty, Surcharges etc. in the overall framework of CENVAT, and thus kept the benefits of comprehensive input tax and service tax set-off out of the reach of manufacturers/ dealers. The introduction of GST will not only include comprehensively more indirect Central taxes and integrate goods and services taxes for set-off relief, but also capture certain value addition in the distributive trade.

Similarly, in the present State-level VAT scheme, CENVAT load on the goods has not yet been removed and the cascading effect of that part of tax burden has remained unrelieved. Moreover, there are several taxes in the States, such as, Luxury Tax, Entertainment Tax, etc. which have still not been subsumed in the VAT. Further, there has also not been any integration of VAT on goods with tax on services at the State level with removal of cascading effect of service tax. In addition, although the burden of Central Sales Tax (CST) on inter-State movement of goods has been lessened with reduction of CST rate from 4% to 2%, this burden has also not been fully phased out. With the introduction of GST at the State level, the additional burden of CENVAT and services tax would be comprehensively removed, and a continuous chain of set-off from the original producer's point and service provider's point upto the retailer's level would be established which would eliminate the burden of all cascading effects, including the burden of CENVAT and service tax.

This is the essence of GST. Also, major Central and State taxes will get subsumed into GST which will reduce the multiplicity of taxes, and thus bring down the compliance cost. With GST, the burden of CST will also be phased out.

Thus GST is not simply VAT plus service tax, but a major improvement over the previous system of VAT and disjointed services tax – a justified step forward.

SALIENT FEATURES OF THE GST MODEL

The salient features of the proposed model are recommended by the Empowered Committee in its 'First Discussion Paper' as follows:

(i) Consistent with the federal structure of the country, the GST will have two components: one levied by the Centre (hereinafter referred to as Central GST), and the other levied by the States (hereinafter referred to as State GST).

This dual GST model would be implemented through multiple statutes (one for CGST and SGST statute for every State). However, the basic features of law such as chargeability, definition of taxable event and taxable person, measure of levy including valuation provisions, basis of classification etc. would be uniform across these statutes as far as practicable.

(ii) The Central GST and the State GST would be applicable to all transactions of goods and services except the exempted goods and services, goods which are outside the purview of GST and the transactions which are below the prescribed threshold limits.

(iii) The Central GST and State GST are to be paid to the accounts of the Centre and the States separately.

(iv) Since the Central GST and State GST are to be treated separately, in general, taxes paid against the Central GST shall be allowed to be taken as input tax credit (ITC) for the Central GST and could be utilized only against the payment of Central GST. The same principle will be applicable for the State GST.

(v) Cross utilisation of ITC between the Central GST and the State GST would, in general, not be allowed.

(vi) To the extent feasible, uniform procedure for collection of both Central GST and State GST would be prescribed in the respective legislation for Central GST and State GST.

(vii) The administration of the Central GST would be with the Centre and for State GST with the States.

(viii) The taxpayer would need to submit periodical returns to both the Central GST authority and to the concerned State GST authorities.

(ix) Each taxpayer would be allotted a PAN linked taxpayer identification number with a total of 13/15 digits. This would bring the GST PAN-linked system in line with the prevailing PAN-based system for Income tax facilitating data exchange and taxpayer compliance. The exact design would be worked out in consultation with the Income-Tax Department.

(x) Keeping in mind the need of tax payers convenience, functions such as assessment, enforcement, scrutiny and audit would be undertaken by the authority which is collecting the tax, with information sharing between the Centre and the States.

CENTRAL AND STATE TAXES TO BE SUBSUMED UNDER GST

The Empowered Committee has recommended that the following Central Taxes to be subsumed under the Goods and Services Tax:

(i) Central Excise Duty

- (ii) Additional Excise Duties
- (iii) The Excise Duty levied under the Medicinal and Toiletries Preparation Act
- (iv) Service Tax
- (v) Additional Customs Duty, commonly known as Countervailing Duty (CVD)
- (vi) Special Additional Duty of Customs - 4% (SAD)
- (vii) Surcharges, and
- (viii) Cesses.

The following State taxes and levies to be subsumed under GST:

- (i) VAT / Sales tax
- (ii) Entertainment tax (unless it is levied by the local bodies).
- (iii) Luxury tax
- (iv) Taxes on lottery, betting and gambling.
- (v) State Cesses and Surcharges in so far as they relate to supply of goods and services.
- (vi) Entry tax not in lieu of Octroi.

Purchase tax: As per First Discussion Paper, Purchase Tax should not be subsumed under GST

Tax on items containing Alcohol: Alcoholic beverages would be kept out of the purview of GST. Sales Tax/VAT could be continued to be levied on alcoholic beverages as per the existing practice.

Tax on Tobacco products: Tobacco products would be subjected to GST with Input Tax Credit (ITC). Centre may be allowed to levy excise duty on tobacco products over and above GST with ITC.

Tax on Petroleum Products: As far as petroleum products are concerned, it was decided that the basket of petroleum products, i.e. crude, motor spirit (including ATF) and HSD would be kept outside GST as is the prevailing practice in India. Sales Tax could continue to be levied by the States on these products with prevailing floor rate. Similarly, Centre could also continue its levies.

Taxation of Services: As indicated earlier, both the Centre and the States will have concurrent power to levy tax on goods and services. In the case of States, the principle for taxation of intra-State and inter State has already been formulated by the Working Group of Principal Secretaries /Secretaries of Finance / Taxation and Commissioners of Trade Taxes with senior representatives of Department of Revenue, Government of India. For inter-State transactions an innovative model of Integrated GST will be adopted by appropriately aligning and integrating CGST and IGST.

RATE STRUCTURE UNDER GST

The Empowered Committee has recommended a two-rate structure –a lower rate for necessary items and items of basic importance and a standard rate for goods in general in 'First Discussion Paper on GST'. There will also be a special rate for precious metals and a list of exempted items. For upholding of special needs of each State as well as a balanced approach to federal flexibility, it is being discussed whether the exempted list under VAT regime including Goods of Local Importance may be retained in the exempted list under State GST in the initial years. It is also being discussed whether the Government of India may adopt, to begin with, a similar approach towards exempted list under the CGST. For CGST relating to goods, the States

considered that the Government of India might also have a two-rate structure, with conformity in the levels of rate with the SGST. For taxation of services, there may be a single rate for both CGST and SGST.

The exact value of the SGST and CGST rates, including the rate for services, will be made known duly in course of appropriate legislative actions.

HIGHLIGHTS OF THE CONSTITUTION (ONE HUNDRED AND FIFTEENTH AMENDMENT) BILL, 2011

This Bill is in line with the First Discussion Paper which was released by the Empowered Committee of the State Finance Ministers in November, 2009. The Bill read with the Statement of Object and Reasons emphasizes the concept of a harmonious structure of taxation of goods and services reflecting its intention to make the Indian market more competitive and stable. The following are the highlights of Constitutional Amendment Bill, 2011

- Parliament and the State Legislatures have been empowered to make laws in respect of GST.
- Inter-state trade or commerce continues to remain the exclusive domain of the Union. Union have exclusive powers to impose tax on supply of goods or services in the course of interstate trade or commerce.
- Supply of goods or services in the course of import deemed to be inter-state supplies for the purposes of GST Union restricted from imposing surcharge on GST for the purposes of the Union.
- Parliament to formulate principles for determining where a supply of goods or services or of both takes places outside the States or are in the course of import into/export from India.
- 'GST' has been defined to mean any tax on the supply of goods or services or both excluding supply of petroleum crude, high speed diesel, motor spirit, natural gas, aviation turbine fuel and alcoholic liquor for human consumption.
- Excise duty, additional excise duties, excise duty levied on medicinal and toilet preparations, service tax, countervailing duty of customs, additional duty of customs in lieu of VAT and central surcharges and cesses subsumed into GST.
- State VAT, entertainment tax (unless levied by local bodies), luxury tax, taxes on lottery, betting and gambling, tax on advertisements, State cesses and surcharge relatable to supply of goods and services and entry tax subsumed into GST
- All goods or services or both except petroleum crude, HSD, motor spirit (i.e. petrol), natural gas, aviation turbine fuel and alcoholic liquor for human consumption to be covered under the ambit of GST regime.
- The Bill proposes the constitution of the 'GST Council' with the Union Finance Minister as its Chairperson, Union Minister of State in charge of Revenue as Member and Finance Ministers of State Governments as Members. One of the members of the Council would be chosen by the members themselves to be the Vice-Chairperson of the Council One third of the total members to form the quorum of the GST Council. Decision to taken on consensus of all members present.
- GST Council to examine issues relating to GST and make recommendations to the Union and the States on taxes, cesses and surcharge which may be subsumed under GST, rates, exemption list and threshold limits etc. GST Council aimed at maintaining the harmonized structure of the goods and services tax
- GST Dispute Settlement Authority comprising of Chairperson (retired Supreme Court Judge/

Chief Justice of High Court) and another two members (experts in the field of law, economics or public affairs) to be constituted. All the members to be nominated by the President GST Dispute Settlement Authority to adjudicate on any dispute or complaint referred to it by the Union or any State Government in case of deviation from the recommendations of the GST Council.

LESSON ROUND UP

This lesson covered the concept of Goods and Service Tax and developments from time to time.

- An announcement was made by Shri P. Chidambaram, the then Union Finance Minister in the Central Budget (2007-2008) for the introduction of GST with effect from 1st April 2010.
- The EC released its First Discussion Paper on Goods and Services Tax in India on the 10th of November, 2009.
- Dual GST model was recommended by the Empowered Committee.
- The first discussion paper contains the basic structure and concept of GST.
- The EC also recommended for constitutional amendment as the Constitution does not vest express power either in the Central or State Government to levy a tax on the 'supply of goods and services'. Moreover, the Constitution also does not empower the States to impose tax on imports. Therefore, it is essential to have Constitutional Amendments for empowering the Centre to levy tax on sale of goods and States for levy of service tax and tax on imports and other consequential issues.
- The 115th Constitutional Amendment Bill, 2011 ("Bill") was tabled before the Parliament by the Finance Minister on March 22, 2011. The Bill proposes to amend the Constitution to empower the Union and States to frame laws for levying goods and service tax ("GST") on transactions involving supply of goods and services.

SELF TEST QUESTIONS

1. What is GST? What are the developments taken place under it?
2. Which Central and State taxes would be subsumed under GST?
3. Why a need arises for amendment of Constitution?
4. Which Model is recommended by the Empowered Committee.

SUGGESTED READINGS

1. The Constitution (One Hundred And Fifteenth Amendment) Bill, 2011
2. First Discussion Paper on Goods and Services Tax in India, the Empowered Committee of State Finance Ministers - November 10, 2009

Lesson 12

Value Added Tax: Introduction and Procedural Aspects

LESSON OUTLINE

- Historical Background
- Concept and mechanism of VAT
- Registration procedure
- Invoicing
- Filing of returns
- Set-off and composition Scheme
- Rate of tax
- Computation of VAT
- Assessment
- VAT on Works Contract
- Right to use property
- VAT Audit
- Demand and Refund
- Appeals and Revision of orders
- Appearances before the VAT Authorities
- Lesson Round Up
- Self Test Questions

LEARNING OBJECTIVES

Prior to the introduction of VAT in the Centre and in the States, there was a burden of multiple taxation in the pre-existing Central excise duty and the State sales tax systems. Before any commodity was produced, inputs were first taxed, and then after the commodity got produced with input tax load, output was taxed again. This was causing a burden of multiple taxation (i.e. "tax on tax") with a cascading effect. Moreover, in the sales tax structure, when there was also a system of multi-point sales taxation at subsequent levels of distributive trade, then along with input tax load, burden of sales tax paid on purchase at each level was also added, thus aggravating the cascading effect further. When VAT is introduced in place of Central excise duty, a set-off is given, i.e., a deduction is made from the overall tax burden for input tax. In the case of VAT in place of sales tax system, a set-off is given from tax burden not only for input tax paid but also for tax paid on previous purchases. With VAT, the problem of "tax on tax" and related burden of cascading effect is thus removed. Furthermore, since the benefit of set-off can be obtained only if tax is duly paid on inputs (in the case of Central VAT), and on both inputs and on previous purchases (in the case of State VAT), there is a built-in check in the VAT structure on tax compliance in the Centre as well as in the States, with expected results in terms of improvement in transparency and reduction in tax evasion. For these beneficial effects, VAT has now been introduced in more than 150 countries, including several federal countries. In Asia, it has now been introduced in almost all the countries. The concept of GST is also based on the principle of VAT.

- At the end of this lesson the students will
- Understand the concept of VAT
- Able to compute the VAT Liability
- Be familiar with procedural aspects of VAT such as registration, payment, filing of returns
- Have the understanding of the VAT audit
- Know the role of Company Secretaries under VAT

VAT is a multi stage tax on goods that is levied across various stages of production and supply with credit given for tax paid at each stage of value addition.

HISTORICAL BACKGROUND

With the objective to introduce State-Level VAT in India in the Year 1992, the Government of India constituted a Tax Reform Committee headed by Dr. Raja J. Chelliah. In 1993, the Committee recommended the introduction of VAT in place of existing tax system. Thereafter, the Government appointed NIPFP (National Institute of Public Finance and Policy), New Delhi, as the Nodal Agency to work out the modalities of VAT.

The first preliminary discussion on State-Level VAT took place in a meeting of Chief Ministers convened by Dr. Manmohan Singh, the then Union Finance Minister in 1995. In this meeting, the basic issues on VAT were discussed in general terms and this was followed up by periodic interactions of State Finance Ministers.

For implementing the above decisions, an Empowered Committee of State Finance Ministers was set-up. Thereafter, this Empowered Committee met frequently and got full support from the State Finance Ministers, the Finance Secretaries and the Commissioners of Commercial Taxes of the State Governments as well as Senior Officials of the Revenue Department of the Ministry of Finance, Government of India.

Along with these measures ensuring convergence on the basis issues on VAT, steps were taken for necessary training, computerization and interaction with trade and industry, particularly at the State level. This interaction with trade and industry was specially emphasized. The Empowered Committee of State Finance Ministers on February 8, 2003 again endorsed the suggestion that all the State legislations on VAT should have a certain minimum set of common features. Most of the States came out with their respective draft legislations. Shri Jaswant Singh the then Union Finance Minister, also announced the introduction of VAT from 1st April, 2003 in his 2003-2004 budget speech made on February 28, 2003. Owing to some unavoidable circumstances, VAT could not be implemented w.e.f. April 1, 2003 and also on the revised date June 1, 2003, despite all obstacles, Haryana was the first State to implement VAT w.e.f. April 1, 2003. In rest of the States VAT Laws were at draft stage.

WHITE PAPER

The Empowered Committee of the State Finance Ministers constituted by the Ministry of Finance, Government of India, on the basis of the resolution adopted in the conference of the Chief Ministers on November 16, 1999 under the Chairmanship of Dr. Asim Dasgupta came out with a White Paper on State-Level VAT, which was released on January 17, 2005 by Shri P. Chidambaram, The Finance Minister, Government of India. On this occasion the Finance Minister remarked:

“This is the first document which has been collectively prepared and put out to the people of the country by the Finance Ministers of all States.... We have formed the rainbow coalition to undertake one of the biggest tax reforms.”

This Paper consists of three parts.

- In Part I, justification of VAT and the background has been mentioned.
- In Part II, main Design of VAT as evolved on the basis of consensus among the States through repeated discussions in the Empowered Committee has been elaborated.
- In Part III, other related issues for effective implementation of VAT have been discussed.

The White Paper specified that registration under the VAT Act shall not be compulsory for the small dealers with gross annual turnover not exceeding ₹5 lakh. However, the Empowered Committee of State Finance

Ministers has subsequently allowed the States to increase the threshold limit for the small dealers to ₹10 lakh, but the concerned State shall have to bear the revenue loss, on account of increase in the limit beyond ₹5 lakh. The VAT Acts are designed so that high value taxpayers should not be spared and on the contrary small dealers should be hassle free from compliance procedures.

Further with the joint efforts of Central and State Governments VAT was implemented by a majority of states with effect from 1st April, 2005.

CONCEPT OF VAT

Introduction of the value added tax (vat) at the central and the state level has been considered to be a major step an important breakthrough in the sphere of indirect tax reforms in India. The value added tax (vat) in India is a state level multi-point tax on value addition which is collected at different stages of sale with a provision for set-off for tax paid at the previous stage i.e., tax paid on inputs. It is to be levied as a proportion of the value added (i.e. Sales minus purchase) which equivalent is to wages plus interest, other costs and profits. It is a tax on the value added and can be aptly defined as one of the ideal forms of consumption taxation since the value added by a firm represents the difference between its receipts and cost of purchased inputs. As against the old regime of sales tax under which goods are charged to tax at single point, or multi-point on the value of the goods, without any credit being given for taxes paid at the preceding stages. Vat intends to tax only the value added at each stage and not the entire invoice value of the product. By ensuring that only the incremental value is taxed, vat aims at eliminating the cascading effect of taxes on commodities, and thereby reduces the eventual cost to the consumer.

VAT has been introduced by 30 States / UTs. However, Central Sales Tax will continue to govern inter-State Sales and Exports.

REGISTRATION

Every dealer up to the retailer level is required to be registered with the Sales Tax department to avail the credit of input tax. However, there would be a threshold turnover level. The retailers with turnover below the threshold can opt not to register, but pay a nominal composition tax. However, such dealers are not entitled to take credit of prior stage tax, nor can they pass the credit to their buyers. In effect, the VAT chain breaks at their stage. Those opting not to register under VAT can opt for general registration.

Registration of dealers with gross annual turnover above the threshold limit will be compulsory. There will be provision for voluntary registration for dealers with gross annual turnover of less than the threshold limit. All existing dealers will be automatically registered under the VAT Act. A new dealer will be allowed 30 days time from the date of his being liable to get registered.

INVOICE

This entire design of VAT with input tax credit is crucially based on documentation of tax invoice, cash memo or bill. Every registered dealer, having turnover of sales above an amount specified, shall issue to the purchaser [who is entitled to tax credit and not to the final consumer] serially numbered tax invoice with the prescribed particulars. This tax invoice will be signed and dated by the dealer or his regular employee, showing the required particulars.

COMPOSITION AND SET OFF SCHEME

Small dealers with gross annual turnover not exceeding the threshold limit will not be liable to pay VAT. States will have flexibility to fix threshold limit within ₹10 lakh. Small dealers with annual gross turnover not exceeding ₹25 lakh who are otherwise liable to pay VAT, shall however have the option for a composition

scheme with payment of tax at a small percentage of gross turnover. The dealers opting for this composition scheme will not be entitled to input tax credit.

The objective of all such composition schemes is not to burden small dealers by the provisions of record keeping. Therefore, such schemes will generally contain the following features:

- (i) small amount of tax shall be payable;
- (ii) there shall be no requirement to calculate taxable turnover;
- (iii) a simple return form to cover longer return period shall be sufficient.

RETURNS

The return filing procedures are designed in such a way that the compliance costs are minimum. A registered dealer shall be required to file a return along with the requisite details such as output tax liability, value of input tax credit, payment of VAT.

Under VAT there exist simple forms of returns, which shall be filed monthly or quarterly or annually as per the provisions of various State laws. Returns shall be accompanied with the challans evidencing payment of tax. In certain States, returns cum challan forms have been devised. In those cases, the returns along with the payment have to be filed with the treasury.

Every return so furnished is required to be scrutinized expeditiously within the prescribed time limit from the date of filing the return. If any technical mistake is detected on scrutinizing, the dealer shall be required to rectify the defect or pay the deficit respectively.

VAT return is the most important form in VAT administration. It provides the basis for the assessment by the VAT authority and the means for collecting the tax. The first essential aspect in any VAT administration is that the filing of returns is strictly enforced on all VAT dealers and the tax declared is collected. Failure to take action in these areas may render VAT audits ineffective.

RATES OF TAX

Four Types of VAT Rates: As contrasted to the multiplicity of rates under the existing regime, VAT will have 4 broad rates.

- 0% (Exempted) for unprocessed agricultural goods, and goods of social importance), 1% for precious and semiprecious metals,
- 4% for inputs used for manufacturing and on declared goods, capital goods and other essential items,
- 20% for demerit/luxury goods and
- the rest of the commodities will be taxed at a Revenue Neutral Rate of 12.5%.

CREDIT AND SET-OFF UNDER VAT

VAT aims at providing set-off for the tax paid earlier and this is given effect through the concept of input tax credit.

Input tax credit in relation to any period means setting the amount of input tax by a registered dealer against the amount of his output tax.

Tax paid on the earlier point is termed as, "input tax". This amount is adjusted against the tax payable by the purchasing dealer on his sales. This credit availability is called input tax credit.

Input tax is the tax paid or payable in the course of business on purchase of any goods made from a registered dealer of the State.

Output tax means the tax charged or chargeable under the Act, by a registered dealer for the sale of goods in the course of business.

In simple words, input tax is the tax a dealer pays on his local purchases of business inputs which include raw materials, capital goods as well as other inputs used directly or indirectly in his business. Output tax is the tax that a dealer charges on his sales that are subject to tax.

The following are points for consideration while availing input tax credit:

- The input tax credit is to be given for both manufacturers and traders for purchase of inputs/ supplies meant for both sale within the State as well as to other States, irrespective of when these were utilized or sold. This also reduces immediate tax liability.
- Input tax paid in excess of 2% on stock transfers to other states will be eligible for tax credit.
- Input tax credit is allowable to a registered dealer for purchase of any goods made within the State from a dealer holding a valid certificate of registration under the Act. Input tax credit on capital goods is available for traders and manufacturers.
- No input credit on CST paid on purchases from other states. Central sales tax paid on inter-state purchases is not eligible for being set off against Value Added Tax payable in the state.
- Input tax in case of export sales: Export sales are zero rated and thereby exporters are either granted refund of input taxes paid by them or they can adjust such input tax while making domestic sales.
- Input tax on capital goods: While taxes paid on raw materials and inputs are eligible for set off against taxes on output, taxes paid on capital goods are not eligible for immediate set-off. The reason perhaps is the huge credit that States may have to grant in cases of capital purchases of large value. Due to this, tax on capital goods may be granted, but over a certain period of time.
- Input tax credit on capital goods will be available to both traders and manufacturers. Tax credit on capital goods may be adjusted over a maximum of 36 equal monthly installments or the number of installments as may be decided by the state. Other than this a negative list of capital goods based on principles decided by the Empowered Committee which is not eligible for input tax credit.
- Input tax credit of Central Excise and Service Tax: Excise duty and service tax are levied by the Central Government. Whereas VAT is levied by the state government. Hence, Cenvat credit of excise and service tax paid on input goods/input services is allowed while making the payment of excise duty and service tax. However, the credit of the excise duty and service tax is not allowed from VAT liability. This is the reason the GST is proposed.
- In some cases, the input tax paid and taken credit of, may have to be reversed as such, for example, when the material is consumed for personal purposes and not for business purposes, or when the input including packing materials is used for manufacture and/or sale as exempt goods etc.

PURCHASES NOT ELIGIBLE FOR INPUT TAX CREDIT

Input tax credit is generally given for the entire VAT paid within the state on purchases of taxable goods meant for resale or manufacture of taxable goods. However, generally no credit is available in respect of purchases given below:

- (i) Goods purchased from unregistered dealers;

- (ii) Goods purchased from registered dealers who opt for composition scheme;
- (iii) Goods purchased from other states or countries;
- (iv) Purchases of goods used in manufacture of exempted goods;
- (v) Purchases of goods used in manufacture of goods to be dispatched outside any state as branch transfer or consignments;
- (vi) Purchases of goods in cases where the dealer does not have invoices showing amounts of tax charged separately by the selling dealer;
- (vii) Purchase of goods used for personal purposes/consumption or provided free of charge or gifts.
- (viii) Purchase of goods where the purchase invoice is not available with the claimant.
- (ix) Goods purchased are given away as free samples;
- (x) Goods purchased are destroyed by fire or are stolen or lost;
- (xi) Goods purchased and returned within the specified period;
- (xii) Purchase of automobiles and its spare parts and accessories by a person other than a dealer.

EXEMPTED SALE

When a certain sale is exempted from tax, the dealer effecting the exempt sale will not be entitled to any VAT credit on the inputs purchased by him. The sale effected by him will also be exempt from any tax. This results in breaking of the VAT chain.

SAMPLES OR GIFTS

Another example where reversal will be required is when goods are sold as samples or gifts i.e., non-taxable transactions and the input tax credit relating thereto has already been availed against output tax payable on other sale transactions. In such circumstances, the credit earned will be reversed. This is called "Reverse Credit of Input Tax".

CONSIGNMENT TRANSFER

Stock/Consignment transfers are exempt from VAT as these were never under the purview of the State Tax Acts. The input tax paid on such commodities or on the inputs that go into producing such commodities can be taken credit to the extent of excess of input tax over and above 2%. Thus, if the input used in the commodity that is transferred, or the product itself when purchased, was taxed at say 10%, credit can be taken by the transferring dealer to the extent of 8% against other taxable dispatches.

Imported goods will continue to be exempt from VAT on imports. Under VAT, there is no place for Entry taxes and Octroi.

ZERO RATING

Zero Rating means that the tax payable on sale of a commodity is fixed at 0%. Though apparently, it looks similar to an exempted transaction, there is a significant difference between the two. While in an exempted transaction, the tax paid on input lapses i.e. it cannot be set off, under the Zero rated sales, prior stage tax is set off against the 0% tax paid, and effectively the entire tax paid on purchases is eligible for refund. Thus, 'Zero Rating' is advantageous to the dealer compared to 'exempting' of sale transactions. Generally, export sales are zero rated and thereby, exporters are granted refund of taxes paid by them on their inputs. Exporters gain significantly due to the 'Zero Rating'.

WORK CONTRACT TAX

Some contracts are contracts for labour, work or service and not for sale of goods, though goods are in use in executing the contract for labour, work or service e.g., when a contractor constructs a building, the buyer pays for cost of building material labour and other services offered by the contractor. Property in the building is passed on to the buyer and there is no contract for supply of building material as such.

It is quite difficult to establish whether particular contract is 'contract for work' or contract of sale. For this any rigid test is not possible. It depends upon the main object of the parties, circumstances and custom of trade. Generally a contract of sale is a contract whose main object is to transfer of property in and delivery and possession of a chattel as a chattel to the buyer. In the case *Vanguard Rolling Shuttles v. CST AIR 1977 CS 1505*, the supreme has observed that it is very difficult to lay down any universal technique to determine what is contract of sale or what job contract is. In a recent case *ACC Limited v. CC AIR 2001 SC 862*. The Supreme Court held that even if the dominant intention of the contract is rendering of service which will amount to a works contract after 46th Amendment to the Constitution. The State would now be empowered to levy sale tax on material used in such contract.

In the case *Cooch Bihar Contractors Association v. State of West Bengal (1996) 103 STC 477 (SC)*, it was held by the Hon'ble Court if contractor has to pay royalty and property gets transferred to him, it can be included for the purpose of work contract Act.

Many High courts have held that C Form can be issued for purchase of goods which are used in works contract. The dealer is entitled to registration and he can receive sales tax forms in respect of his sales. Central Sales Tax will be payable on goods involved in works contract if goods moved from one state to another on account of such works contract from 11.5.2002 onwards.

There can certainly be inter-state works contract in case of movable property e.g., printing contracts. In fact CST can be levied on any goods involved in works contract in case of movable property.

COMPUTATION AND METHODS OF VAT

VAT can be computed by using any of the three methods detailed below:

1. **The Subtraction method:** Under this method the tax rate is applied to the difference between the value of output and the cost of input;
2. **The Addition method:** Under this method value added is computed by adding all the payments that are payable to the factors of production (viz., wages, salaries, interest payments, etc.);
3. **Tax Credit method:** under this method, it entails set-off of the tax paid on inputs from tax collected on sales. Indian states opted for tax credit method, which is similar to Cenvat.

Illustration

Compute the invoice value to be charged and amount of tax payable under VAT by a dealer who had purchased goods for ₹1,20,000 and after adding for expenses of ₹10,000 and a profit of ₹15,000 had sold out the same.

The rate of VAT on purchases and sales is 12.5%.

Solution**Computation of VAT Payable**

	₹
Goods purchased for (VAT @ 12.5%, ₹ 15,000)	1,20,000
Add: Expenses	10,000
Add: Profit	<u>15,000</u>
	1,45,000
Add: VAT @ 12.5%	<u>18,125</u>
Invoice Value	<u>1,63,125</u>
VAT Payable	= Output Tax – Input Tax
	= ₹ 18,125 – ₹ 15,000
	= ₹ 3,125

Note: It is assumed that purchase price is exclusive of VAT.

Illustration

Porwal Traders have provided the following information relating to purchase and sales for the month of July, 2011 :

Purchases:

Product "A" total cost ₹1,80,000, rate of VAT 4%.

Product "B" total cost ₹2,60,500, rate of VAT 12.5%.

Sales:

Product "A" total sales ₹2,40,000, rate of VAT 4%.

Product "B" total sales ₹2,10,000, rate of VAT 12.5%.

On the basis of above information, compute eligible input tax credit and value added tax payable for the month.

Solution**Calculation of Input VAT credit and VAT payable
for the month of July 2011**

	₹
VAT payable on sale of	
Product A ₹2,40,000 x 4%	9,600
Product B ₹2,10,000 x 12.5%	<u>26,250</u>
Total VAT payable for the month	35,850

Less: Input Tax Credit (eligible) on Purchase:

Product A ₹1,80,000 x 4%	7,200
Product B ₹2,60,500 x 12.5%	<u>32,563</u>
	39,763
Net VAT Payable	Nil

Balance of Input Tax Credit available (39,763 – 35,850) = 3,913 can be carried forward to the next month and utilised against future sales.

Illustration

Ramesh, a trader sells entire raw material to a manufacturer of finished products in the same State. He buys his stock in trade from other States as well as from the local markets. Following transactions took place during the financial year 2011-12:

	₹
Cost of materials purchased from other States	
including central sales tax @2%	3,06,000
Cost of local materials including VAT	6,75,000
Other expenditure includes storage, transport, interest, loading and unloading and profit earned by him	2,62,500

Calculate VAT and invoice value charged by him to the manufacturer. Assume the rate of VAT @ 12.50%.

Solution**Calculation of VAT and Invoice Value**

	₹
Cost of material imported from other state	3,00,000
CST on above @ 2%	6,000
Cost of local material excluding VAT ($₹6,75,000 \times 100 \div 112.5$)	6,00,000
Other expenditure and profit margin	<u>2,62,500</u>
Total	11,68,500
Add: VAT @ 12.5%	<u>1,46,063</u>
Invoice Value	<u>13,14,563</u>

VAT payable = VAT liability minus input tax credit i.e. ₹ 71,063 (₹1,46,063 – ₹ 75,000)

ASSESSMENT

The VAT liability shall be self-assessed by the dealer himself. The aim of the VAT system is to encourage the highest level of voluntary compliance using system of self-assessment. The Dealer calculates his own liability and makes his payment of the tax due while the Commercial Taxes Department reviews the self-assessment subsequently by means of a VAT audit to ensure that tax legally due is declared and paid by the tax payers.

A self-assessment system relies for its effectiveness on a number of integrated components. They are:

- Maintenance of proper books of account and records by all VAT dealers
- An effective system of periodic audits targeted at the 'at risk' category of VAT dealers and supplemented by physical checks
- A proper taxpayer education campaigns so that VAT dealers are aware of their obligations
- Simple, understandable and effective procedures and forms so that a Dealer can easily comply without undue cost.
- Deterrent penalties for non-compliance which are enforced by the Commercial Taxes Department
- Simple and effective controls which reduce the scope for fraud.
- Prompt and effective action against VAT dealers who have not filed VAT returns and/or who have not paid the tax declared or assessed.

VAT AUDIT

Audit is one of the four important pillars of vat administration, the other three being registration, returns and refunds. The word 'audit' encompasses both the functionalities of inspection and assessment. In the context of self-assessment system under vat, the function of audit acquires paramount importance. The main objective of audit for bridging the gap between the tax due and the tax declared by the dealers.

In many of the state audit of accounts by Accountant or other specified person is mandatory if the turnover exceeds the specified limit in a year.

REFUNDS

Refunds are to be granted by the end of the financial year. Thus, the benefit of zero rating is not immediate, but deferred. Some States have also provided for refund where the tax paid on inputs exceeds the output tax payable and cannot be set off in a given period. In such cases, the excess tax not so set off shall be refunded after adjusting any dues towards interest, penalty, etc., in accordance with the State VAT Act.

SCRUTINY PROCESS

The correctness of self assessment will be checked through a system of departmental audit. It is a sample audit by which a certain percentage of assessees or dealers are taken on scientific basis for audit purposes. If it is found that some of the dealers deliberately defalcated their dues for the particular Financial Year then the department will carry out audit of previous financial years. The audit wing is separated from the collection wing in order to ward off any kind of biasness. The entire audit process is conducted in a transparent way and such process should be completed within six months. The audit report should be provided to the dealer and other concerned persons. Simultaneously a cross checking computerized system is also being used in coordination with tax authorities of the State Governments and the authorities of Central Excise and Income Tax to compare the tax returns and set off documents of VAT system of the states and those of Central Excise and Income Tax. This comprehensive cross checking will help to reduce tax evasion and also lead to significant growth in tax base of the country.

APPEALS, REVISION AND APPEARANCES

As we know that in India there is no central Value Added Tax Act till now. The reason being sales tax is state subject found in List II of the Seventh Schedule of our Constitution. As a result the Central Government cannot use their prerogative to institute in a Central Act governing VAT in our country. There is no consensus among states to introduce a unique Act which will apply to all states and union territories without any reservation and constraints. The eventuality is being separate states have their own VAT Act and those states which do not have the relevant Act are in the process of making them. The States making those Acts is according to their own conveyance and likings which serves their interest more profoundly. Since different states and union territories have their own VAT Act and Rules, the appeal, revision and other relevant issues are explained differently. As a result any representative provisions relating to appeals, revision and appearances cannot be stated. It is worth mentioning that some states have recognised till now company secretaries as authorised representative to represent their client's case before any VAT authority. The states are West Bengal, Gujarat, Bihar, Goa and Karnataka. Other states are in the process of recognizing company secretaries as professionals who can appear before their respective VAT authorities.

ROLE AND POSITION OF COMPANY SECRETARIES

As we know that the VAT system in India is not unique and every state and Union Territories have its own VAT Act or Rules; it becomes quite a difficult task to give a generalized picture regarding Certification of Documents by professionals applicable to all states or union territories. However, considering the above

situation, in general terms a professional including a Company Secretary, has to see that all documents to be filed before VAT authorities are correct or not. Specially the calculation sheet, tax calculation sheet, TIN or GRN No., etc. Apart from this the Company Secretary has to see the returns to be filed before VAT authorities are made in prescribed rules. He is also taken into consideration the procedural aspects regarding payment of VAT and related assessment proceedings.

As a professional he has to see that whether the dealer has maintained the records and documents required under the Act. He has to advise the concerned client the provisions relating to appeals and revisions if any matter relating to VAT proceedings is undertaken by Appellate Tribunal or Court of Law as the case may be.

Company Secretary has also be well versed with the technical aspects in dealing with seizure and confiscation procedure before judicial or quasi judicial bodies. Besides this a professional dealing with VAT authorities has to carefully vouch and take careful steps with regard to books of accounts, and return procedures annually.

Every state has its own peculiarities regarding to documents to be filed before the VAT authorities in connection with filing of return and other related issues. The technicalities and calculation of tax is an important component of services is to be provided by professional under VAT authorities in India. Any mistakes or errors can put the client in great displeasure and anxiety.

The profession of Practicing Company Secretaries, which made a humble beginning in the sixties, has now reached greater heights. With the blended knowledge of various laws, the Practicing Company Secretaries are versatile professionals capable of rendering wide range of services in diversified fields including VAT.

(1) AUTHORIZED REPRESENTATIVE BEFORE VAT AUTHORITIES

The Company Secretaries play poignant role in their professional capacity before VAT authorities in our country. The acceptability of company secretaries before the VAT authorities is increasing day by day. Company Secretaries in Practice have now been recognized to act as an authorized representative for the purpose of appearing before VAT authorities under Statutes of various States. The Company Secretaries in Practice have been recognized to act as Authorized Representative under -

- (i) Maharashtra Value Added Tax Act, 2002 –Section 82(1)(b)
- (ii) Delhi Value Added Tax Act, 2004 – Section 82(1)(b)
- (iii) West Bengal Value Added Tax Rules, 2005 – Rule 2(1)(a)(iv)
- (iv) Bihar VAT Act, 2005 – Section 87(d)
- (v) Goa VAT Act, 2005 – Section 82(1)(b)
- (vi) Karnataka VAT Rules, 2005 – Rule 168(1)
- (vii) Kerala VAT Act, 2003 – Section 86(e)
- (viii) Daman & Diu VAT Regulation, 2005 – Regulation 82(1)(b)
- (ix) Jharkhand VAT Rules, 2006 – Rule 51(1)(c)

The Company Secretaries in Practice have been recognized to act as Authorized Representative under the VAT Laws of the other states also via Section 288 of the Income Tax Act, 1961 read with Rule 50 of the Income Tax Rules, 1962.

(2) CERTIFICATION OF DOCUMENTS

Moreover, the VAT system in India is not unique and every state and Union Territories have its own VAT Act or Rules; it becomes quite a difficult task to give a generalized picture regarding Certification of Documents

by professionals applicable to all states or union territories. A professional including a Company Secretary, has to see that all documents to be filed before VAT authorities, specially the calculation sheet, tax calculation sheet, TIN or GRN No., etc.

(3) FILING OF RETURNS

The Company Secretary has to see the returns to be filed before VAT authorities are made in prescribed rules. He should also consider the procedural aspects regarding payment of VAT and related assessment proceedings. Every state has its own peculiarities regarding the documents to be filed before the VAT authorities in connection with filing of return and other related issues.

(4) SCRUTINY OF RECORDS AND ADVISING TO CLIENTS

As a professional he has to see that whether the dealer has maintained the records and documents required under the Act. He has to advise the concerned client the provisions relating to appeals and revisions if any, matters relating to VAT proceedings is undertaken by Appellate Tribunal or Court of Law as the case may be.

Company Secretary has to be well versed with the technical aspects in dealing with seizure and confiscation procedure before judicial or quasi judicial bodies. Besides this a professional dealing with VAT authorities has to carefully vouch and take careful steps with regard to books of accounts, and return procedures annually. The technicalities and calculation of tax is an important component of services to be provided by professional under VAT authorities in India.

VAT AUDIT

The Company Secretaries in Practice have been recognized to conduct VAT Audit under the following States:

- Jharkhand VAT Act, 2005 – section 2(i).
- Karnataka VAT Rules, 2005 – As a Tax Practitioner under Rule 34(1)
- Gujarat VAT Act, 2005 – As a Tax Practitioner under Rule 59(1)(a)

LESSON ROUND UP

- The Value Added Tax (VAT) in India is a state level multi-point tax on value addition which is collected at different stages of sale with a provision for set-off for tax paid at the previous stage i.e., tax paid on inputs. It is to be levied as a proportion of the value added (i.e. sales minus purchase) which equivalent is to wages plus interest, other costs and profits. It is a tax on the value added and can be aptly defined as one of the ideal forms of consumption taxation since the value added by a firm represents the difference between its receipts and cost of purchased inputs.
- Registration of dealers with gross annual turnover above the threshold limit will be compulsory.
- There will be provision for voluntary registration for dealers with gross annual turnover of less than the threshold limit.
- The return filing procedures are designed in such a way that the compliance costs are minimum. A registered dealer shall be required to file a return along with the requisite details such as output tax liability, value of input tax credit, and payment of VAT.
- When a certain sale is exempted from tax, the dealer effecting the exempt sale will not be entitled to any VAT credit on the inputs purchased by him

- VAT aims at providing set-off for the tax paid earlier and this is given effect through the concept of input tax credit.
- Some contracts are contracts for labour, work or service and not for sale of goods, though goods are in use in executing the contract for labour, work or service e.g., when a contractor constructs a building, the buyer pays for cost of building material labour and other services offered by the contractor.
- There shall no longer be compulsory assessment at the end of each year. Correctness of self-assessment shall be checked through a system of Department Audit. A certain percentage of the dealers shall be taken up for audit every year on a scientific basis

SELF TEST QUESTIONS

1. Discuss the provisions of registration under VAT.
2. How would you take input tax credit when goods purchased are transferred by the dealer to his branch in any other State?
3. "A registered dealer can set-off the amount of input tax against the amount of his output tax." Explain.
4. Explain the procedure of registration under 'value added tax' (VAT).
5. In what purchases input tax credit is not allowed under VAT?
6. What are the deficiencies in the design of VAT that has been adopted by the States in India? Give your opinion.
7. "Tax credit or invoice method has been adopted universally because of the inherent advantages in the credit method of calculating tax liability." Explain.
8. Discuss, with suitable example, various methods for computation of VAT liability.
9. Discuss the role of Company Secretaries in the professional capacity before VAT authorities in our country.

SUGGESTED READINGS

1. Dr. V. K. Singhania: Students Guide to Income-tax; Taxmann Publications Pvt. Ltd., New Delhi.
2. Girish Ahuja and Ravi Gupta: Systematic Approach to Income-tax and Sales-tax; Bharat Law House, New Delhi.

PROFESSIONAL PROGRAMME
ADVANCED TAX LAWS AND PRACTICE

PP-ATLP

TEST PAPERS

A Guide to CS Students

To enable the students in achieving their goal to become successful professionals, Institute has prepared a booklet 'A Guide to CS Students" providing the subject specific guidance on different papers and subjects contained in the ICSI curriculum. The booklet is available on ICSI website and students may download from <http://www.icci.edu/Portals/0/AGUIDETOCSSTUDENTS.pdf>

WARNING

It is brought to the notice of all students that use of any malpractice in Examination is misconduct as provided in the explanation to Regulation 27 and accordingly the registration of such students is liable to be cancelled or terminated. The text of regulation 27 is reproduced below for information:

"27. Suspension and cancellation of examination results or registration

In the event of any misconduct by a registered student or a candidate enrolled for any examination conducted by the Institute, the Council or the Committee concerned may suo motu or on receipt of a complaint, if it is satisfied that, the misconduct is proved after such investigation as it may deem necessary and after giving such student or candidate an opportunity to state his case, suspend or debar the person from appearing in any one or more examinations, cancel his examination result, or studentship registration, or debar him from future registration as a student, as the case may be.

Explanation - Misconduct for the purpose of this regulation shall mean and include behaviour in a disorderly manner in relation to the Institute or in or near an Examination premises/centre, breach of any regulation, condition, guideline or direction laid down by the Institute, malpractices with regard to postal or oral tuition or resorting to or attempting to resort to unfair means in connection with the writing of any examination conducted by the Institute".

PROFESSIONAL PROGRAMME
ADVANCED TAX LAWS AND PRACTICE

TEST PAPER 1

(This Test Paper is for recapitulate and practice for the students. Students need not to submit responses/answers to this test paper to the Institute.)

Time Allowed: 3 hours

Maximum Marks: 100

NOTE: All the references to sections mentioned in Part-A of the Question Paper relate to the Income-tax Act, 1961 and relevant Assessment Year 2014-15, unless stated otherwise.

PART A
(Direct Taxation—Law and Practice)

1. A and B are two partners (1:2) of XY co., a firm engaged in the manufacturing of chemicals. The profit and loss accounts of the firm for the year ending 31.3.2014 are as follows:

Particulars	Amount(₹)	Particulars	Amount (₹)
Cost of goods sold	86,00,000	Sales	1,26,00,000
		Long term capital gains	80,000
		Other business receipts	62,000
Salary to staff	17,79,600		
Depreciation	1,60,000		
Remuneration to partners:			
A	6,00,000		
B	4,80,000		
Interest on capital to partners @ 18%			
A	72,000		
B	50,400		
Other expenses	7,40,000		
Net profit	2,60,000		
Total	1,27,42,000		1,27,42,000

Other information:

- (1) The firm completed all legal formalities to get the status of a 'Firm'.
- (2) The firm has given donation of ₹ 1,60,000/- to a notified public charitable trust which is included in other expenses.
- (3) Salary and interest is paid to the partners as per the partnership deed.
- (4) Depreciation allowable under section 32 is ₹1,56,000/-
- (5) Income and investment of X and Y are as follows:

	X (₹)	Y (₹)
Interest on company deposit	1,28,000	1,01,600
Dividend from foreign companies	14,000	22,000
Long term capital gains(loss)	1,60,000	40,000
Short term capital gains(loss)	6,000	(12,000)
Winning from lotteries(gross)	8,000	20,000
Contribution towards home loan a/c of national Housing Bank	80,000	1,20,000

Find out Net Income and tax liability of the firm and partners for the Assessment year 2014-15.

(15 marks)

Attempt all parts of either Q.No. 2 or Q.No. 2A

2. (a) Explain how is the residential status of a company determined under the Income Tax Act, 1961? (5 marks)

- (b) Explain provisions relating to 'advance ruling' in the Income Tax Act, 1961. (10 marks)

OR

(Alternate Question to Q. No. 2)

- 2A. (a) Discuss the scope of the provisions, Central Government may make under section 90A(1) of the Income Tax Act-1961, in respect of agreement between specified association. (5 marks)

- (b) What do you understand by "Book Profit" in the context of Minimum Alternate Tax? (5 marks)

- (c) Explain how the arm's length price in relation to an international transaction is computed under the comparable uncontrolled price method as per rule 10B of the Income Tax Rules, 1962. (5 marks)

PART B
(Central Excise, Customs, VAT & Service Tax)

3. (a) What do you mean by reverse charge mechanism in Service Tax? Give examples where such mechanism is applicable. (10 marks)

- (b) Briefly state the provisions relating to the procedure of registration under Service Tax. (10 marks)

- (c) Mr. X is providing taxable as well as exempted services. The value of taxable services is ₹10 lakh while that of exempted services is 14 lakh. All the input/output services used by him are commonly used in providing taxable as well as exempted services for which separate account are not maintained. The total input credit is ₹4 lakh. Find the amount payable by Mr. X as per Rule 6(2). (5 marks)

Attempt all parts of either Q.No. 4 or Q.No. 4A

4. (a) Compute the assessable value of excisable goods, for levy of duty of excise, given the following information –

Cum-Duty wholesale price including sales tax of ₹2,500	15,000
Normal secondary packing cost	1,000
Cost of special secondary packing	1,500
Cost of durable and returnable packing	1,500
Freight	1,250
Insurance on freight	200

Trade discount (normal practice)	1,500
Rate of Central Excise duty as per Central Excise Tariff	10% Ad valorem
(5 marks)	

- (b) What is special audit under section 14AA of Central Excise Act, 1944? (5 marks)
- (c) State the provisions of transshipment of goods without payment of duty under section 54 of Customs Act, 1962. Explain briefly. (5marks)

OR

(*Alternate Question to Q. No. 4*)

- 4A. (a) From the following information, compute the amount of basic customs duty and additional duty of customs payable under section 3(1) of the Customs Tariff Act, 1975 in respect of import of readymade garments:
- Assessable value under customs: ₹ 1,50,000/-
 - Tariff value notified under Central excise for levy of excise duty : 45% of the retail sale price;
 - Retail sale price : ₹4,00,000/- (readymade garments are not notified under section 4A of the Central Excise Act, 1944);
 - Basic customs duty; 10%
 - Central Excise duty : 10%; and
 - Education cess: as applicable.
- (5 marks)
- (b) Write short note on:
- (i) Unjust Enrichment in Central Excise Law
 - (ii) Anti Dumping duty.
- (5 marks each)
5. (a) What is "Composition scheme" under VAT. Discuss various features of composition scheme. (5 marks)
- (b) Explain the different methods for computation of VAT. (5 marks)
- (c) Determine the taxable turnover, input tax credit and net VAT payable by a works contractor from the detail given below on the assumption that the contractor maintains sufficient records to quantify the labour charges. Assume output VAT as 12.5%:

	₹ (In lakh)
Total contract price (excluding VAT)	100
Labour charges paid for execution of the contract	35
Cost of consumables used not involving transfer of property in goods	5
Material purchased and used for the contract taxable at 12.5% VAT (VAT included)	45

The contractor also purchased a plant for use in the contract for ₹10.4 lakhs. In the VAT invoice relating to the same VAT, was charged at 4% separately and the said amount of ₹10.4 lakhs is inclusive of VAT. Assume 100% Input credit on capital goods.

Make suitable assumptions wherever required and show the working noted. (5 marks)

6. (a) What are the provisions relating to filling of return under the Service Tax Laws? (5 marks)
- (b) What is meant by "manufacture" under the Central Excise Act, 1944? Explain by giving reference to the relevant case laws.
- (c) XYZ Ltd., imported a machine at a FOB value of ₹17,00,000. This sum includes ₹2,00,000 attributable to post-importation activities to be carried out by the seller. XYZ Ltd., had supplied raw material worth ₹5,00,000 to the seller for the manufacture of the said machine. The goods

were imported by vessel and actual cost of transportation is ₹80,000. The importer has also paid demurrage charges of ₹5,000 and lighterage and barge charges of ₹15,000, in addition to the transportation charges. Further the importer also paid ₹25,000 for transportation of goods from port of entry to Inland Container Depot. The actual cost of insurance is ₹50,000. Compute assessable value. *(5 marks)*

TEST PAPER 2

(This Test Paper is for recapitulate and practice for the students. Students need not to submit responses/answers to this test paper to the Institute.)

Time Allowed: 3 hours

Maximum Marks: 100

NOTE: All the references to sections mentioned in Part-A of the Question Paper relate to the Income-tax Act, 1961 and relevant Assessment Year 2014-15, unless stated otherwise.

PART A
Direct Taxation Management

1. (a) Explain the provisions of MAT under the Income Tax Act, 1961. (10 marks)
- (b) "Tax evasion is the result of suppression, misrepresentation, illegality and fraud". Explain. (5 marks)

Attempt all parts of either Q. No. 2 or Q. No. 2A

2. (a) What do you mean by Arm's Length Price? What are the methods of calculating it? (5 marks)
- (b) The applicability of transfer pricing provision has been extended to 'specified domestic transaction'. List down the transactions covered under section 92BA as 'specified domestic transaction'? (5 marks)
- (c) Write a brief note on "Foreign Direct Investment (FDI)". (5 marks)

OR

(Alternate Question to Q. No. 2)

- 2A. (a) How foreign institutional investors are taxed on the income and the capital gains arising from the transfer of securities? Discuss. (10 marks)
- (b) What do you mean by 'foreign tax credit'? Explain. (5 marks)

PART B
(Central Excise, Customs, VAT & Service Tax)

- 3.(a) What is the due date for payment of service tax and the interest on delayed payment of service tax as specified under section 75? (5 marks)
- (b) Discuss 'advance ruling in service tax'. (5 marks)
- (c) Compute the amount of service tax in the following cases, assuming the applicable rate of service tax to be 12.36%
 - (i) A goods carriage carrying 5 consignments (all belonging to different persons) at fare of ₹300 each.
 - (ii) A goods carriage carrying 10 consignments (all belonging to different persons) at fare of ₹500 each.
 - (iii) A goods carriage carrying 5 consignments (booked by five different persons but addressed to the same consignee) at fare of ₹300 each.
 - (iv) A goods carriage carrying 5 consignments (booked by five different persons but addressed to the same consignee) at fare of ₹400 each. (10 marks)
- (d) What is VAT invoice? What are the mandatory provisions to be complied with while issuing a VAT invoice by a registered dealer? (5 marks)

Attempt all parts of either Q. No. 4 or Q. No. 4A

4. (a) Calculate the assessable value and total customs duty payable from the following particulars
- (i) Date of presentation of bill of entry: 20.06.2013 (Rate of BCD 10%, Exchange Rate ₹43.60 and rate notified by CBEC ₹43.80).
 - (ii) Date of arrival of goods in India: 30.06.13 [Rate of BCD 10%; Exchange Rate ₹43.90 and rate notified by CBEC ₹44.00.
 - (iii) Rate of additional Customs Duty: 14%.
 - (iv) CIF value 2,000 US Dollars; Air Freight 500 US Dollars, Insurance cost 100 US Dollars [Landing Charges not ascertainable]
 - (v) Education cess applicable @2% and SHEC is 1%. Assume there is no special CVD.
- (5 Marks)
- (b) Differentiate between:
- (i) Exempted Goods and Nil Rated Goods
 - (ii) Remission of Duty and Abatement of duty under Central Excise Act, 1944. (5 marks each)

OR

(Alternate Question to Q. No. 4)

- 4A. (a) Compute assessable value for Central Excise purposes of Product A whose details are given below. Out of 1,000 units manufactured, 800 units of product A have been cleared to a sister unit for further production of excisable goods on assessee's behalf; the balance 200 units are lying in stock—

	₹
Direct Material consumed (inclusive of excise duty @ 8.24%)	2,16,480
Direct Labour & Director Expenses	1,80,000
Works Overheads (inclusive of Quality Control costs of ₹25,000 and Research & Development Costs of ₹75,000)	1,60,000
Administrative Overheads (60% related to production)	1,50,000
Packing Cost of primary as well as secondary packing	40,000
Net value of non-excisable inputs received free of cost from sister unit for manufacture of A	80,000
Value of moulds, dies, etc. Received free of cost from sister unit for manufacture of A (25% of the value relates to current production)	2,00,000
Interest and financial charges	86,000
Abnormal losses (not included above)	14,000
VRS compensation to labour/employees (not included above)	1,00,000
Selling and Distribution Costs (including advertisement)	36,000
Reliable value of Scrap/Wastage	10,000

(5 marks)

- (b) How is the assessable value determined when the excisable goods are not sold for delivery at the time and place of removal? (5 marks)
- (c) Distinguish between "Identical Goods" and "Similar good" with reference to Custom Valuation Rules, 2007. (5 marks)

5. (a) R Ltd. of Gujarat made total purchases of input and capital goods for ₹55,00,000 during the month of October, 2013. The following information is given below:
- (i) Goods worth ₹15,00,000 were purchased from Tamil Nadu on which CST @ 2% was paid.
 - (ii) The purchase made in October, 2013 include goods purchased from un-registered dealers amounting to ₹18,50,000.
 - (iii) Also purchased are capital goods for ₹6,50,000 (not eligible for input tax credit) and those eligible for input tax credit for ₹9,00,000.

Sales made in the state of Gujarat for ₹10,00,000 on which VAT is levied @12.50% during the month of October 2013. All purchases are exclusive of tax and VAT is levied @ 4%. Calculate net VAT liability. (5 marks)

- (b) Enumerate any five purchases not eligible for input tax credit. (5 marks)
 - (c) Explain the provisions for claiming drawback of duty paid on imported goods when they are re-exported. (5 marks)
6. (a) Explain the meaning of "Baggage". What is the relevant date for determination of rate of duty and tariff valuation in case of a baggage? (5 marks)
- (b) What are the clearances whose value are excluded for the purpose of calculating the Small Scale Exemption Limit (SSI) while calculating the turnover of 150/400 lakhs? (5 marks)
 - (c) Write a short note on Adjustment of excess amount of service tax paid. (5 marks)
-