Report of the Comptroller and Auditor General of India

for the year ended March 1997

Union Government

(Indirect Taxes-Central Excise)

No.11 of 1998

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PREFATORY REMARKS

This Report for the year ended 31 March 1997 has been prepared for submission to the President under Article 151 of the Constitution, based on the audit of Central Excise Receipts of the Union of India, in terms of Section 16 of the Comptroller and Auditor General's (Duties, Powers and Conditions of Service) Act, 1971.

The cases mentioned in the Report are among those which came to notice in the course of audit during the year 1996-97 and early part of the year 1997-98, as well as those which came to notice in earlier years but were not reported earlier.

ABBREVIATIONS/LEGENDS

1.	A.C.	Refer as	Assistant Commissioner of Central Excise
2.	Commissioner	-do-	Commissioner of Central Excise
3.	Commissionerate	-do-	Commissionerate of Central Excise
4.	CVD	-do-	Countervailing Duty
5.	Duty	-do-	Central Excise Duty
6.	Government	-do-	Central Government
7.	HSC	-do-	Harmonized System Committee
8.	HSN	-do-	Harmonized Commodity Description and Coding System Explanatory Notes
9.	Modvat	-do-	Modified Value Added Tax
10.	MRP	-do-	Maximum retail price
11.	PLA	-do-	Personal Ledger Account
12.	SCN	-do-	Show Cause Notice
13.	SSI	-do-	Small Scale Industry
14.	The Act	-do-	Central Excise Act, 1944
15.	The Board	-do-	Central Board of Excise and Customs
16.	The Industrial Act	-do-	The Industries (Development and Regulation) Act, 1951
17.	The Ministry	-do-	Ministry of Finance
18.	The Rules	-do-	Central Excise Rules, 1944
19.	Tariff	-do-	Schedule to the Central Excise Tariff Act, 1985
20.	The Tariff Act	-do-	Central Excise Tariff Act, 1985
21.	The Valuation Rules	-do-	Central Excise Valuation Rules, 1975
22.	VABAL	-do-	Value Based Advance License

OVERVIEW

This report contains 374 paragraphs, featured individually or grouped together and two reviews having a financial implication of Rs.3531.78 crore. Some of the more significant findings are mentioned below:

I. GENERAL

The net receipts from excise duty during the year 1996-97 was Rs.44,818 crore against the budget estimates of Rs.46,883 crore, resulting in shortfall of Rs.2,065 crore. In case of top 22 major revenue yielding commodities, the variation between actual receipts and budget estimates ranged from (-) 24.23 per cent to (+) 62.29 per cent, though the rates of duty on these commodities (except plastics and fabrics of man made staple) remained constant. It was noticed that in the case of cement, motor vehicles and synthetic filament yarn, the actual receipts were lower than the budget estimates though the production during 1996-97 increased by 10, 15 and 31 per cent (respectively) over the previous year's production. Further, in the case of synthetic filament yarn the actual receipts in 1996-97 were lower than the actual receipts in 1995-96 by 22 per cent and the budget estimates by 5.5 per cent though the production from this sector registered an increase by 31 per cent (from 776100 tonne in 1995-96 to 1012745 tonne in 1996-97).

(Paragraph 1.1. and 1.5)

While the value of production had increased by 9.8 times between 1980-81 and 1996-97, the central excise receipts went up by only 6.9 times during the corresponding period. The central excise receipts were 11.2 per cent of the value of production in 1980-81 but had decreased to 7.9 per cent in 1996-97.

(Paragraph 1.3)

The increasing trend in availing Modvat credit could be explained mainly due to the expansion of the scheme to cover most of the excisable goods including

capital goods, This also indicates the misuse of Modvat credit as indicated through paragraphs 2, 4.4 and 9 of this Audit Report.

(Paragraph 1.4)

50687 cases involving Rs.56395.17 crore of central excise duty were pending for finalisation with different authorities, as on 31 March 1997.

(Paragraph 1.8)

II. SYSTEM APPRAISAL

Modvat credit on capital goods

An appraisal of the system of Modvat credit on capital goods, introduced from 1 March 1994, revealed an incorrect availment of Modvat credit of Rs.249.58 crore in 1051 cases, with a further revenue loss of Rs.68.47 crore, by way of non-recovery of interest. Some of the major irregularities were as follows:

⇒ **393 assessees availed credit of Rs.66.07 crore on ineligible items.**

(Paragraph 2.5)

⇒ **112 assessees availed credit of Rs.52.12 crore even before the capital goods were installed or put to use.**

(Paragraph 2.6)

⇒ **Modvat credit of Rs.25.75 crore was availed in contravention of the provisions in the Act/Rules for (i) capital goods utilised for inadmissible purposes, (ii) goods which did not fall under the definition of capital goods, (iii) goods on which depreciation for the duty element had already been claimed under Income Tax Act and (iv) goods on which valid duty paying documents were not available.**

(Paragraph 2.7 to 2.10)

⇒ **Modvat credit of Rs.49.50 crore was allowed to be availed by 70 assessees, even in the absence of requisite declarations or the delays in filing such returns having been condoned.**

(Paragraph 2.11)

⇒ **Delay in issue of show cause notices and their adjudication resulted in loss of revenue of Rs.9.91 crore and blocking up of revenue of Rs.395.54 crore with loss of interest of Rs.43.19 crore.**

(Paragraph 2.12 and 2.13)

⇒ **69 assessees though required, did not submit 22637 duty paying documents involving Modvat credit of Rs.86.47 crore for defacement, in the absence of which the genuineness of the duty paying documents could not be verified.**

(Paragraph 2.14)

Soap and detergent

Commodity specific appraisal of central excise duty collections from 'soap and detergent' revealed escapement/short levy of duty of Rs.121.75 crore. Some of the important findings were as follows:

⇒ **Lacuna in the existing Act/Rules, enabled certain major manufacturers/brand name owners to get their products manufactured and cleared by other manufacturers (job workers) at an agreed price much lower than the prices of their own similar products or the prices at which these goods were finally cleared in the wholesale market, thereby depriving the Government of Rs.68.25 crore. There is, therefore, a need to levy duty on `soaps' in terms of maximum retail price.**

{Paragraph 3.5(i)}

⇒ **Government was deprived of a revenue of Rs.7.55 crore due to reduction in the assessable value without justification, which was also not subject to any checks by the department, under the 'invoice based assessments'.**

{Paragraph 3.5(ii)}

⇒ **Rs.6.03 crore of excise duty could not be levied due to acceptance by the department of incorrect classification of products like 'preparations for use on hair' and 'dish wash bars' etc.**

{Paragraph 3.6(i) and (ii)}

⇒ **Despite the restriction imposed by the Drug Controller (India) on marketing of soaps having a 'total fatty matter (TFM)' content of less than 60 per cent as 'toilet soaps', the department allowed 'beauty/bathing bars' with less than the required percentage of 'TFM' to be cleared as 'toilet soap'.**

{Paragraph 3.6(iii)}

⇒ **Absence of suitable provisions in the Act/Rules to (i) levy interest for delay in payments from the date of clearances of goods and (ii) have time limits for finalisation of assessment/adjudication, led to non-recovery of duty of Rs.43.00 crore and loss of Rs.19.79 crore by way of interest.**

(Paragraph 3.9)

III NON-LEVY/SHORT LEVY OF DUTY

- **Short levy/underassessment of central excise duty amounting to Rs.3091.98 crore (excluding those in system appraisals) were noticed. The more significant of these findings were as follows:**

(Paragraph 1.15)

⇒ **Four units of public sector corporations, in Rajkot Commissionerate, collected excise duty of Rs.661.22 crore on the sale of petroleum products but did not remit it to the Government.**

(Paragraph 4.1)

⇒ **Delay in implementation of ad valorem rates of duty on 'tyres and tubes' and non-revision of specific rates in consonance with the rising prices of tyres, resulted in short collection of revenue of Rs.1767.71 crore in four units alone.**

(Paragraph 4.2)

⇒ **Non-revision of tariff value of aerated waters in bottles of size upto 1000 ml. and non-fixation of tariff value of bottles of size exceeding 1000 ml., resulted in loss of revenue of Rs.33.69 crore.**

(Paragraph 4.3)

⇒ **Inconsistent approach of the Ministry/department in treating a product as non-excisable for the purpose of valuation and excisable for allowing Modvat credit, resulted in incorrect availment of Modvat credit of Rs.18.64 crore.**

(Paragraph 4.4)

⇒ **Non-raising of demands for duty or delay in adjudication of demands or non-realisation of confirmed demands, resulted in non-recovery/loss of revenue amounting to Rs.160.07 crore.**

(Paragraph 5)

⇒ **Non-maintenance of production records for coconut oil by a manufacturer, led to escapement of duty of Rs.42.24 crore.**

(Paragraph 6.1)

⇒ **Application of exemption notifications on goods not correctly entitled to these exemptions, resulted in short collection of duty of Rs.50.70 crore.**

(Paragraph 7)

⇒ **Incorrect valuation of excisable goods resulted in short levy of duty of Rs.35.27 crore.**

(Paragraph 8)

⇒ **Incorrect availment of credit under Modvat scheme on inputs or short reversal of credit by advance licencees, resulted in the Government being deprived of Rs.31.47 crore.**

(Paragraph 9)

⇒ **Incorrect classification of excisable goods resulted in short levy of duty of Rs.28.91 crore.**

(Paragraph 10)

⇒ **Abnormal delay in finalisation of provisional assessment cases led to loss of revenue of Rs.191.22 crore by way of interest and blockage of Government revenue of Rs.44.18 crore.**

(Paragraph 14.1)

⇒ **Board's instructions to the detriment of revenue in the assessment of 'dant manjan lal' resulted in loss of revenue of Rs.1.83 crore.**

(Paragraph 14.2)

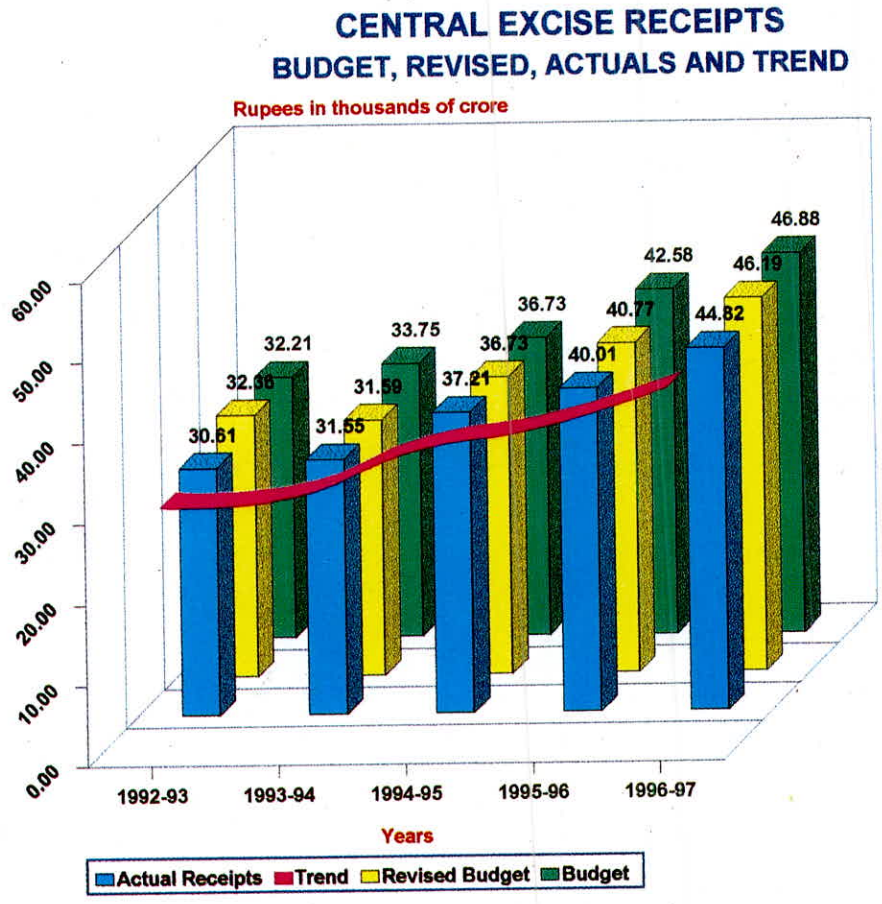
1. CENTRAL EXCISE RECEIPTS

1.1 Budget estimates, actual receipts and their trend

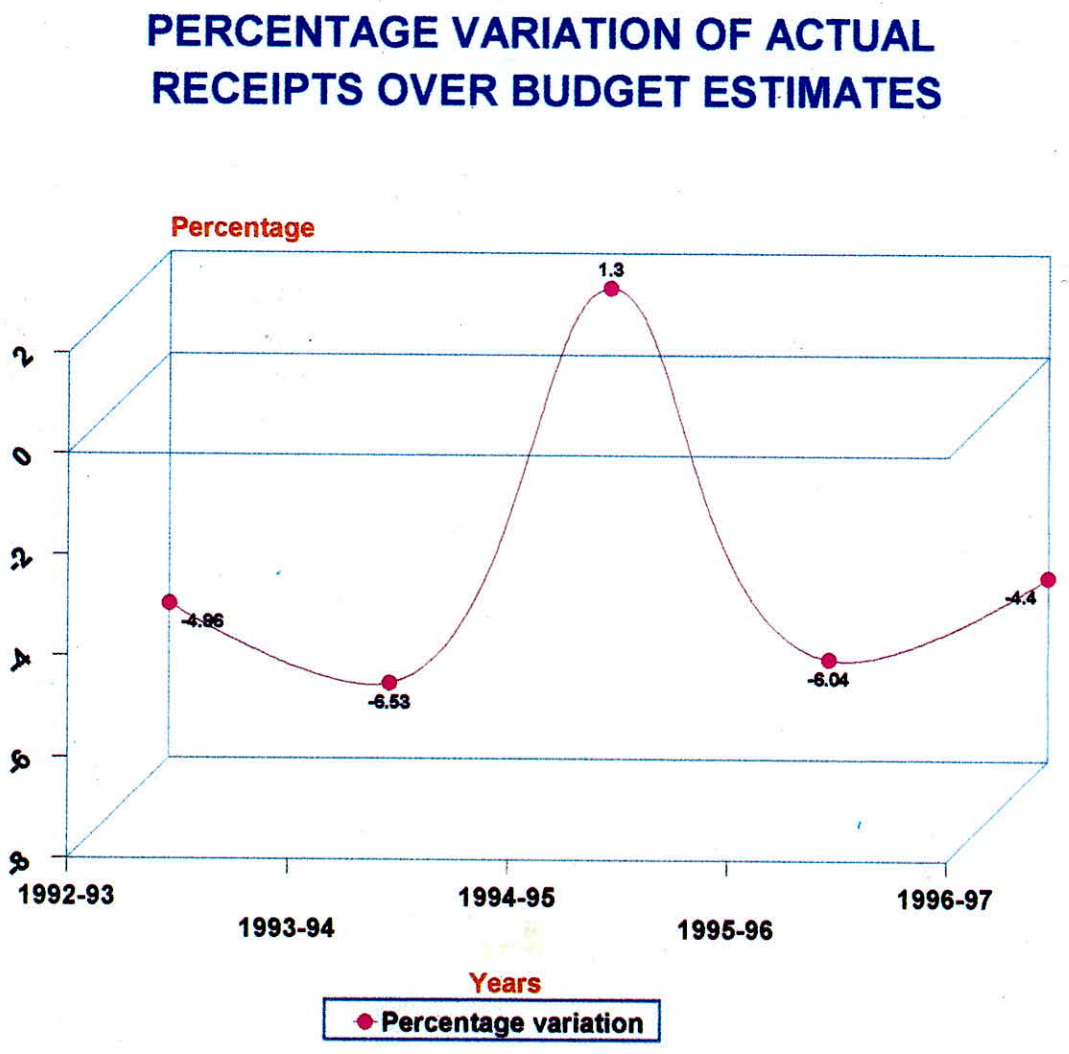
a) The budget estimates, actual receipts of central excise duties and the trend of receipts during the year 1996-97 alongwith the corresponding figures for preceding four years are given in the table and the graph:-

Year	Budget estimates	Revised budget estimates	Actual receipts	Difference between actual receipts and budget estimates	Percentage variation
	(Amount in crore of rupees)				
1992-93	32,211	32,357	30,614	(-) 1597	(-) 4.96
1993-94	33,751	31,591	31,548	(-) 2203	(-) 6.53
1994-95	36,732	36,732	37,208	(+) 476	(+) 1.30
1995-96	42,579	40,767	40,009	(-) 2570	(-) 6.04
1996-97	46,883	46,190	44,818	(-) 2065	(-) 4.40

Note : Figure furnished by Principal Chief Controller of Accounts (Central Board of Excise and Customs)



b) The graph below depicts the percentage variation of actual receipts with reference to budget estimates. Excepting for the year 1994-95, the actual receipts had been lower than the budget estimates all through the years 1992-93 to 1996-97.

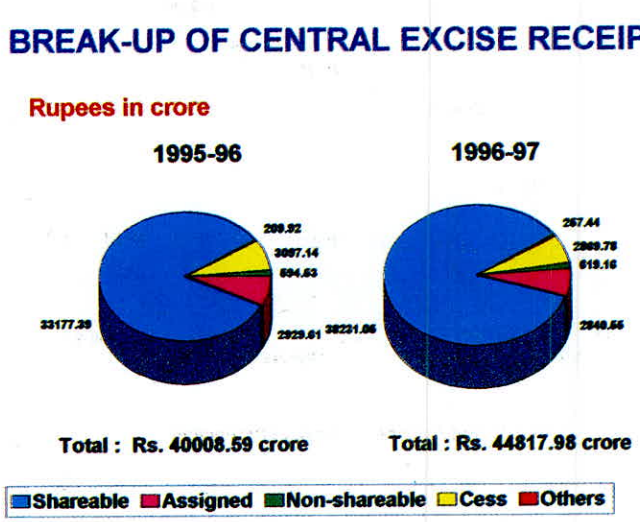


1.2 Break-up of receipts

The receipts during the year 1996-97 from levy of basic excise duties and from other duties levied as excise duties are given in the table and the graph below, alongside the corresponding figures for the preceding year:-

		Receipts from Union Excise Duties 1995-96 (Amount in crore of rupees)	1996-97
A.	**Shareable duties :**		
	Basic excise duties	33158.07	38222.91
	Auxiliary duties of excise	--	0.03
	Special excise duties	19.32	8.08
	Additional excise duties on mineral products	--	0.03
	Total (A)	**33177.39**	**38231.05**
B.	**Duties assigned to states :**		
	Additional excise duties in lieu of sales tax	2929.59	2840.50
	Excise duties on generation of power	0.02	0.05
	Total (B)	**2929.61**	**2840.55**
C.	**Non-shareable duties :**		
	Additional excise duty on T.V. sets	0.04	0.05
	Special excise duties	0.02	1.64
	Additional excise duties on textiles and textile articles	594.47	590.99
	Other duties	--	0.03
	Auxiliary duties of excise	--	26.45
	Total (C)	**594.53**	**619.16**
D.	**Cess on commodities**	**3097.14**	**2869.78**
E.	**Other receipts**	**209.92**	**257.44**
	Total : (A to E)	**40008.59**	**44817.98**

Note : Figure furnished by Principal Chief Controller of Accounts (Central Board of Excise and Customs)



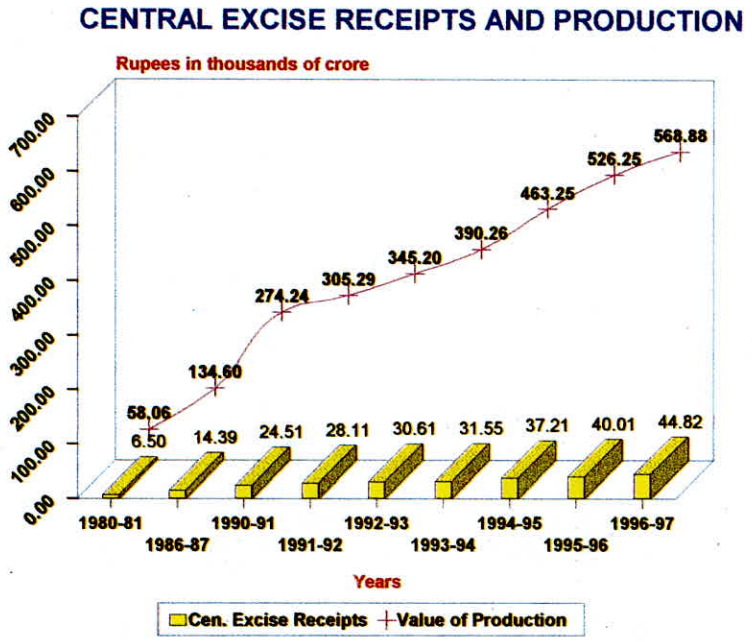
1.3 Value of output vis-a-vis central excise receipts

a) The value of production from manufacturing sector vis-a-vis receipt of central excise duties through PLA (cash collection) during the years 1980-81 and 1986-87 to 1996-97 are given below :

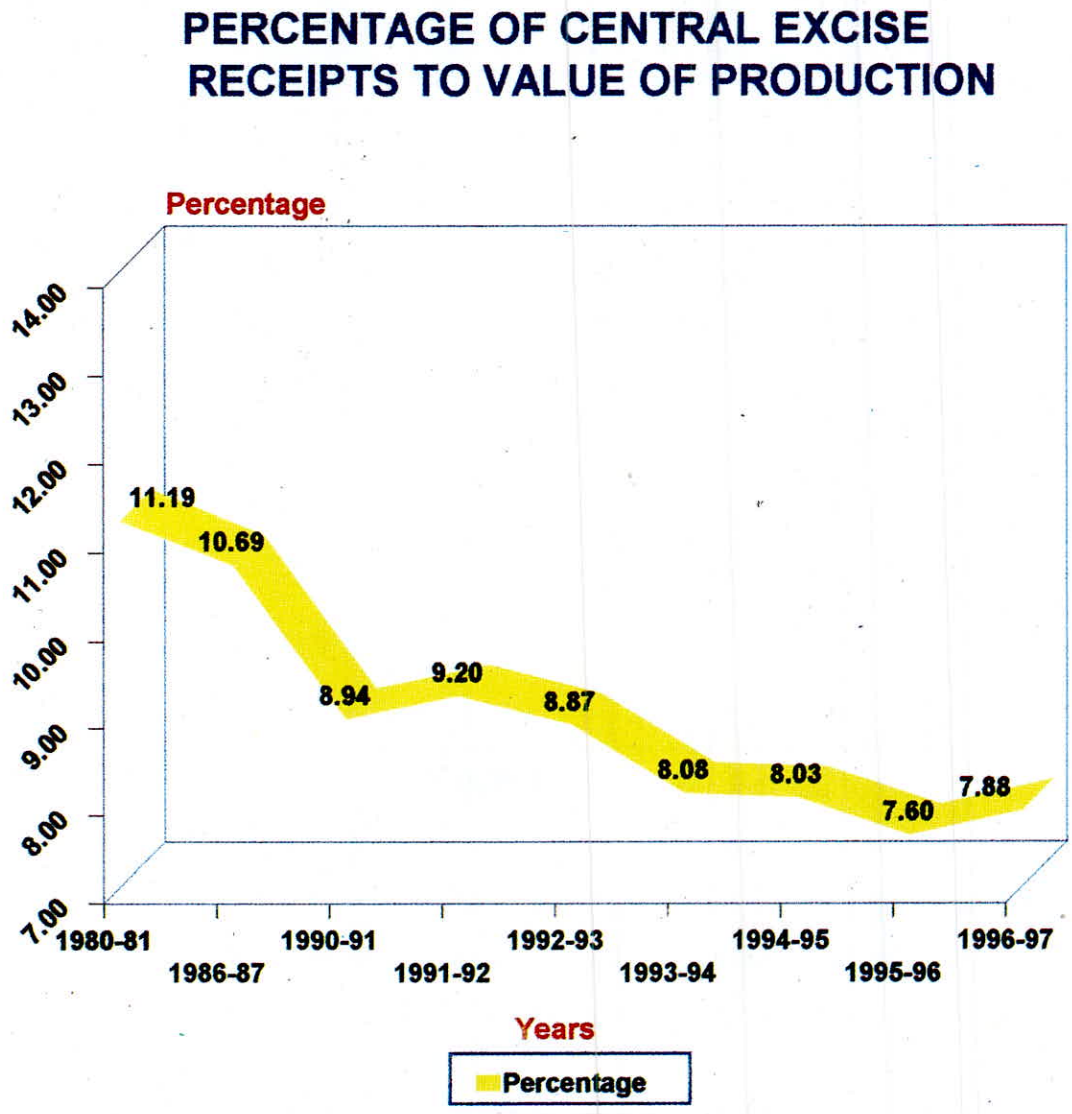
Year	Value of production	Central excise	Percentage of central excise receipts to value of production
	(Amount in crore of rupees)		
1980-81	58065	6500	11.19
1986-87	134602	14387	10.69
1990-91	274241	24514	8.94
1991-92	305293	28110	9.20
1992-93	345204	30614	8.87
1993-94	390259	31548	8.08
1994-95	463250	37208	8.03
1995-96	*526252	40009	7.60
1996-97	*568878	44818	7.88

* Estimated by audit on the basis of figure published by Central Statistical Organisation. As separate figure of value of production by SSI units and for export production were not available, these have not been excluded from the value of production indicated.

The above table and graph below reveal that while value of output had increased by a factor of 9.8 during the period 1980-81 to 1996-97, the corresponding increase in the central excise receipts was by a factor of 6.9 only.



b) The graph below shows a declining trend in percentage of central excise receipts to value of output from 11.19 during 1980-81 to 7.60 during 1995-96 with a marginal increase to 7.88 in 1996-97.



1.4 Central excise receipts vis-a-vis Modvat availed

A comparative statement showing the details of central excise duty paid through PLA, the amount of Modvat availed during the year 1986-87 to 1996-97 is given in the table below:

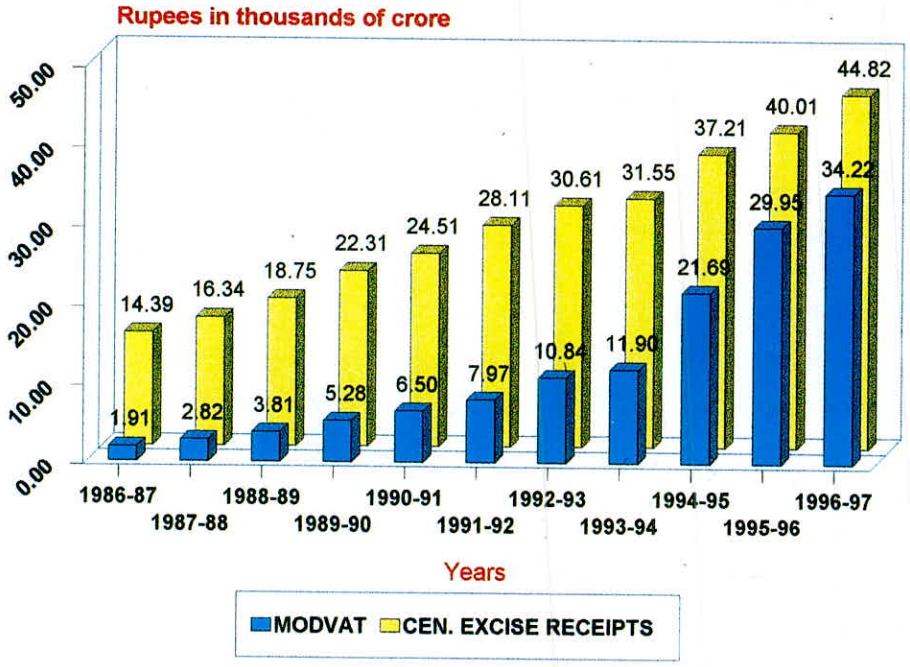
(Amount in crore of rupees)

Year	Central excise duty paid through PLA		Modvat availed		Percentage of Modvat to duty paid through PLA
	Amount	Percentage increase	Amount	Percentage increase	
1986-87	14387	--	1914	--	13.30
1987-88	16345	13.60	2820	47.30	17.25
1988-89	18749	14.70	3809	35.07	20.31
1989-90	22307	18.97	5279	38.59	23.66
1990-91	24514	9.89	6496	23.05	26.49
1991-92	28110	14.66	7965	22.61	28.33
1992-93	30614	8.91	10840	36.09	35.40
1993-94	31548	3.05	11896	9.74	37.70
1994-95	37208	17.94	21687	82.30	58.28
1995-96	40009	7.53	29951	38.10	74.86
1996-97	44818	12.01	34222	14.25	76.35

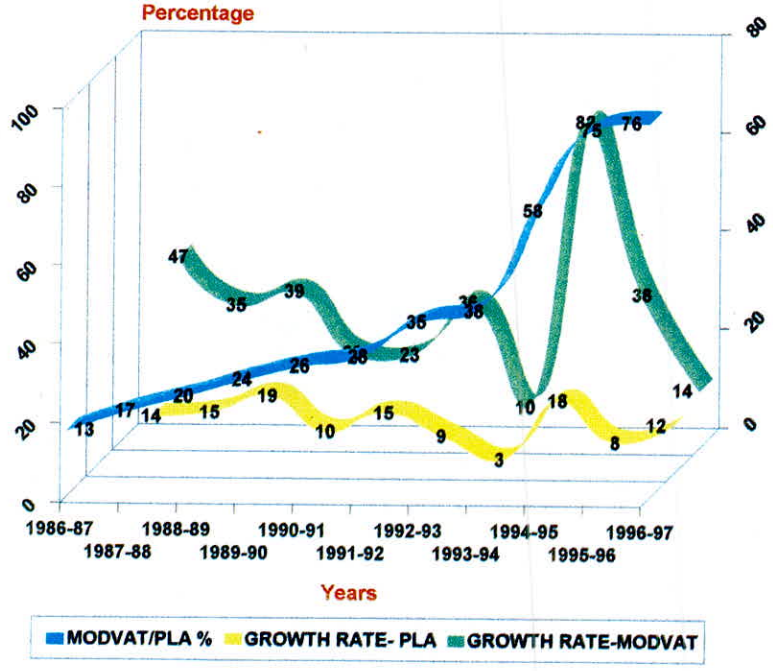
A perusal of the above table and the graphs following would show that while the central excise receipts had grown by 3.12 times during the decade 1986-87 to 1996-97, the increase in Modvat availed during the relevant period had been 17.88 times. It would also be seen that the percentage of Modvat availed to duty paid by cash had been increasing consistently from 13.30 per cent to 76.35 per cent.

The increasing trend in availing Modvat credit can be attributed to the expansion of the scheme to cover most of the excisable goods including capital goods and a certain degree is also indicative of misuse of Modvat credit facility as brought out in paragraphs 2, 4.4 and 9 of this Audit Report.

GROWTH OF CENTRAL EXCISE RECEIPTS (PLA) AND MODVAT AVAILED



RATE OF GROWTH OF PLA AND MODVAT WITH PERCENTAGE OF MODVAT TO PLA



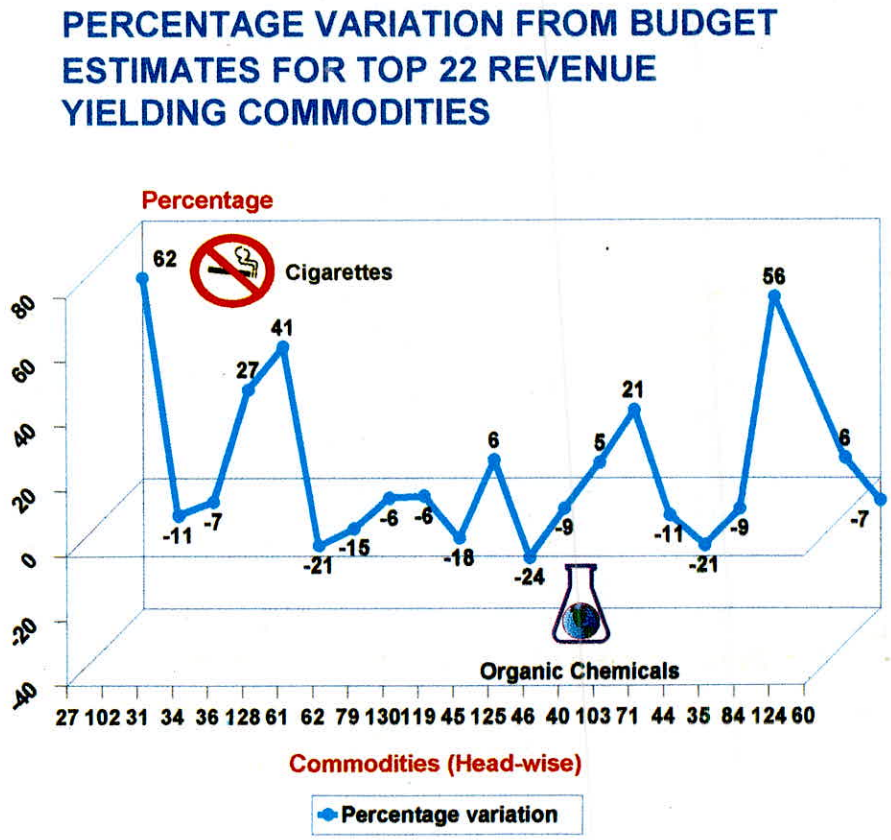
1.5 Major revenue yielding commodities

The commodities (as per budget heads) which yielded revenue of more than Rs.500 crore during 1996-97 alongwith corresponding figures for 1995-96 are as under:

Sl. No.	Budget Head	Description	1995-96 (Actual)	1996-97 (Budget estimates)	1996-97 (Actual)	Percentage variation of actual over budget
			(Amount in crore of rupees)			
1.	27	Cigarettes, cigarillos or tobacco substitutes	3426.87	2454.00	3982.66	(+) 62.29
2.	102	Iron and steel	3540.27	4395.10	3894.80	(-) 11.39
3.	31	Cement clinkers, cement all sorts	2180.49	2459.50	2281.12	(-) 7.26
4.	34	Motor spirit	1631.45	1662.90	2116.79	(+) 27.34
5.	36	Refined diesel oil	1155.19	1395.00	1961.97	(+) 40.64
6.	128	Motor cars and other motor vehicles for transport of persons	1341.57	1856.10	1472.22	(-) 20.68
7.	61	Plastics and articles thereof	1396.79	1703.80	1442.82	(-) 15.28
8.	62	Tyres, tubes and flaps	1286.87	1519.70	1427.10	(-) 6.10
9.	79	Synthetic filament yarn and sewing thread including synthetic monofilament and waste	1782.89	1464.20	1383.51	(-) 5.51
10.	130	All other goods falling under chapter 87 (Vehicles other than Railway)	910.70	1035.40	1225.74	(+) 18.42
11.	119	All other goods falling under chapter 84 (Machinery, Mechanical appliances, Nuclear Reactors)	979.78	1144.00	1207.47	(+) 5.54
12.	45	Organic chemicals	1133.79	1385.00	1049.55	(-) 24.23
13.	125	All other goods falling under chapter 85 (Electrical equipment, sound system, TVs etc.)	878.52	1067.30	970.13	(-) 9.08
14.	46	Pharmaceutical products	720.22	842.15	882.07	(+) 4.75
15.	40	All other goods falling under chapter 27 (Mineral fuels, oils)	733.24	728.10	880.93	(+) 21.00
16	103	Articles of iron and steel	701.54	841.30	746.74	(-) 11.21
17.	71	Paper and paper board, articles of paper pulp or paper or paper board	692.87	841.55	668.60	(-) 20.50
18.	44	All other goods falling under chapter 28 (Inorganic chemicals)	623.08	726.95	658.35	(-) 9.32

Sl. No.	Budget Head	Description	1995-96 (Actual)	1996-97 (Budget estimates)	1996-97 (Actual)	Percentage variation of actual over budget
			(Amount in crore of rupees)			
19.	35	Kerosene	257.62	414.40	646.74	(+) 56.06
20.	84	Fabric of man made staple	631.99	N.A	600.53	--
21.	124	Insulated wire, cable and other electric conductors	498.00	537.60	570.44	(+) 6.10
22.	60	Miscellaneous chemical products	445.21	539.45	502.56	(-) 6.84

The above table and the graph below show that there were wide variations in the actual central excise receipts which ranged from (-) 24.23 per cent in case of 'organic chemicals' to 62.29 per cent in case of 'cigarettes', though the rates of duty on these commodities (except plastics and fabric of man made staple) remained unchanged. It was noticed that in the case of cement, motor vehicles and synthetic filament yarn, the actual receipts were even lower than the Budget estimates though production during 1996-97 increased by 10, 15 and 31 per cent respectively over the previous year's production. Further, in the case of synthetic filament yarn the actual receipts in 1996-97 were lower than the actual receipts in the previous year 1995-96 by 22 per cent and by 5.5 per cent of the Budget estimates for 1996-97 though the production from this sector registered an increase by 31 per cent (from 776100 tonne in 1995-96 to 1012745 tonne in 1996-97).



1.6 Cost of collection

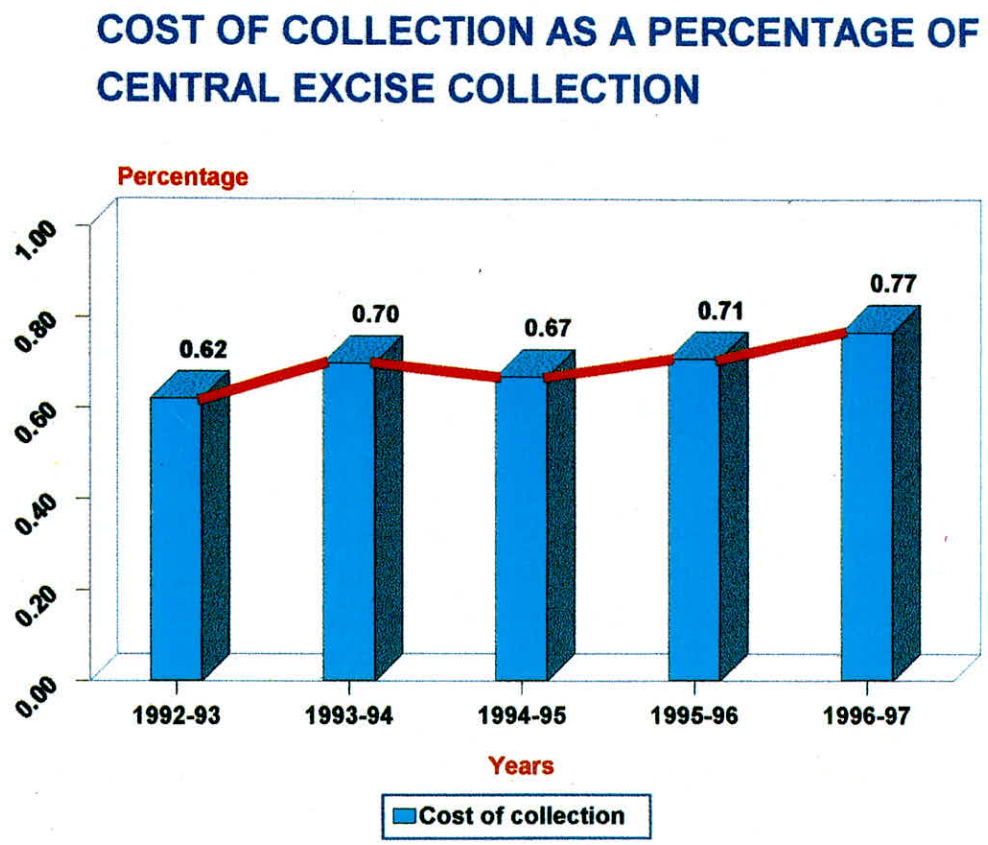
The expenditure incurred during the year 1996-97 in collecting central excise duty alongwith the corresponding figures for the preceding four years is given below:-

(Amount in crore of rupees)

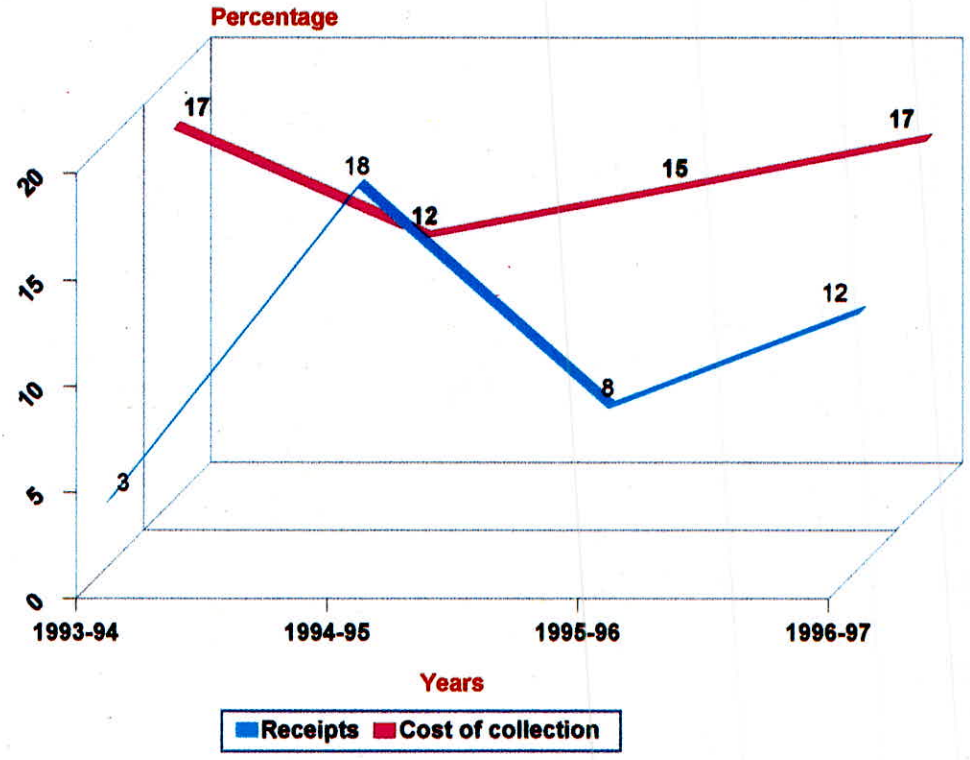
Year	No. of factories paying excise duty	Receipts from excise duty		Expenditure on collection		Cost of collection as percentage of receipts
		Amount	Percentage increase over previous year	Amount	Percentage increase over previous year	
1992-93	84662	30613.55	--	188.67	--	0.62
1993-94	# 54454	31547.61	3.05	221.65	17.48	0.70
1994-95	@ 52409	37207.84	17.94	249.10	12.38	0.67
1995-96	* 39864	40008.59	7.52	285.47	14.60	0.71
1996-97	* 43662	44817.98	12.02	333.82	16.93	0.77

Figure relates to 33 out of 36 Commissionerates
@ Figure relates to 23 out of 36 Commissionerates
* Figure relates to 18 out of 36 Commissionerates
Note: Figure furnished by Principal Chief Controller of Accounts (Central Board of Excise and Customs)

The table above and the graphs following show that excepting for the year 1994-95, the cost of collection as a percentage of the central excise revenue had a rising trend. Further, while the revenue growth had averaged around 10.13 per cent, the expenditure on collection had risen at an average rate of 15.35 per cent.



PERCENTAGE GROWTH IN CENTRAL EXCISE RECEIPTS AND COST OF COLLECTION



1.7 Rebates, refunds and rewards*

i) Rebates

The amount of rebate on excise duty paid on goods exported and excise duty not levied on goods exported during the period 1994-95 to 1996-97 are given below:

		1994-95	1995-96	1996-97
		(Amount in crore of rupees)		
(a)	Rebate under rule 12	42.15	86.25	65.94
(b)	Rebate under rule 12A	3.99	35.89	37.00
(c)	Duty not levied under rule 13 - revenue foregone as a result of export under bond	2380.01	2552.74	2548.57
(d)	Differential duty recovered on unrebated amount on goods exported under bond	0.09	1.72	2.69

ii) Refunds

The amount of duty refunded by the department during the period 1994-95 to 1996-97 is given below:

		1994-95	1995-96	1996-97
		(Amount in crore of rupees)		
i)	Number of cases	2409	3177	3341
ii)	Amount of refunds (other than rebate)	55.91	44.96	557.39
iii)	Interest on refunds			
	(a) No. of cases	02	10	6
	(b) Amount paid	0.095	0.06	0.003

The table above reveals that there had been a steep rise (around 1240 per cent) in amount of refunds during the year 1996-97 over the year 1995-96.

iii) Rewards

The amount of rewards paid to informers and departmental officers and amount of additional duty realised during the period 1994-95 to 1996-97 were as under:-

		1994-95	1995-96	1996-97
		(Amount in crore of rupees)		
(a)	Amount of rewards paid to informers	1.97	4.38	0.20
(b)	Amount of reward paid to the departmental officers	8.69	6.09	0.72
(c)	Additional duty realised as a result of payment of rewards	186.58	301.43	1.74

* Figure relates to 21 out of 36 Commissionerates

1.8 Outstanding demands *

The number of cases and amount involved in demands for excise duty, outstanding as on 31 March 1996 and 31 March 1997 are given below:

(Amount in crore of rupees)

		As on 31 March 1996				As on 31 March 1997			
		Number of cases		Amount		Number of cases		Amount	
		More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years	More than five years	Less than five years
(a)	Pending with Adjudicating officers	6164	15478	635.89	2246.56	971	30186	817.46	21782.55
(b)	Pending before								
(i)	Appellate Commissioners	185	936	60.71	210.34	171	1972	31.58	490.78
(ii)	Board	511	968	33.87	168.10	403	999	25.00	89.86
(iii)	Government	110	23	1.64	3.26	40	13	22.86	9.54
(iv)	Tribunals	1608	2853	3472.35	1375.20	1582	4091	3212.59	5064.51
(v)	High Courts	406	410	500.87	228.13	539	636	11292.79	7628.22
(vi)	Supreme Court	203	72	38.67	32.90	312	120	3496.19	805.91
(c)	Pending for coercive recovery measures	15566	1920	48.49	141.35	5771	2881	705.71	919.69
	Total	24753	22660	4792.50	4405.84	9789	40898	19604.11	36791.06

It may be seen that 50687 cases involving demands amounting to Rs.56395.17 crore were pending on 31 March 1997 with different authorities. Further, number of cases pending even with the adjudicating authorities had increased from 21642 during 1995-96 involving Rs.2882.45 crore to 31157 cases amounting to Rs.22600 crore during 1996-97.

1.9 Revenue lost on grounds of limitation *

The amount of demands for duty, barred by limitation due to demands not having been raised in time, during the last three years was Rs.1137.60 lakh, as detailed below:

Year	Amount in lakh of rupees
1994-95	13.46
1995-96	197.27
1996-97	926.87

* Figure relates to 21 out of 36 Commissionerates

The above data reveals that increasing amount of revenue had been lost due to departmental inaction.

1.10 Revenue remitted or abandoned *

Amount of central excise duty remitted/abandoned or written off due to various reasons for the year 1995-96 and 1996-97 is shown below:

(Amount in lakh of rupees)

		1995-96		1996-97	
		Number of cases	Amount	Number of cases	Amount
	Remitted due to :				
(a)	Fire	25	6.76	34	6.51
(b)	Flood	3	0.70	3	1.89
(c)	Theft	--	--	--	--
(d)	Other reasons	16	29.59	16	7.27
	Total	44	37.05	53	15.67
	Abandoned or written off due to :				
(a)	Assessees having died leaving behind no assets	9	0.02	1	0.05
(b)	Assessees untraceable	133	2.08	10	0.10
(c)	Assessees left India	--	--	--	--
(d)	Assessees incapable of payment of duty	7	0.20	6	0.04
(e)	Other reasons	4	0.33	30	2.00
	Total	153	2.64	47	2.19

* Figure relates to 21 out of 36 Commissionerates

1.11 Seizures, confiscation and prosecution *

The number and amount involved in the cases of seizures, confiscation and prosecution relating to excise duty during the last two years are given below:

(Amount in lakh of rupees)

		1995-96		1996-97	
		Number	Amount	Number	Amount
i)	**Seizure cases**				
(a)	initiated	1224	10292.91	1550	11784.86
(b)	decided in favour of the assessees	114	1948.80	79	1869.02
(c)	decided in favour of the department	314	1431.31	247	651.46
(d)	pending decisions	652	4769.56	880	8108.93
ii)	**Goods seized**	391	6567.89	425	8465.51

(Amount in lakh of rupees)

		1995-96		1996-97	
		Number	Amount	Number	Amount
iii)	**Goods confiscated**				
(a)	in seizure cases	388	9921.24	113	381.06
(b)	in non-seizure cases	54	134.00	62	188.00
iv)	**No. of offences prosecuted**				
(a)	arising from seizure	57	1114.50	23	353.00
(b)	arising otherwise	40	256.90	139	268.84
v)	**Duties assessed in respect of goods seized or confiscated**	619	2349.51	386	4589.42
vi)	**Fines levied**				
(a)	on seizure and confiscated cases	392	419.71	168	150.13
(b)	in other cases	95	22.90	17	7.39
vii)	**Penalties levied**	410	585.11	289	576.60
viii)	**Goods destroyed after confiscation**	32	4.11	6	5.11
ix)	**Goods sold after confiscation**	2	8.00	2	5.00
x)	**Prosecution resulting in conviction**	6	14.14	8	3.78

* Figure relates to 21 out of 36 Commissionerates

1.12 Provisional assessments *

The number of cases of provisional assessments and amount involved therein, as on 31 March 1996 and 31 March 1997 is depicted below:

(Amount in crore of rupees)

		As on 31 March 1996		As on 31 March 1997	
		Number of cases	Duty involved	Number of cases	Duty involved
(a)	Pending decision by Court of Law	91	483.61	51	414.96
(b)	Pending decision by Government of India or Central Board of Excise and Customs	16	686.89	14	721.83
(c)	Pending adjudication with the Commissioners	565	702.69	399	90.62
	Total	672	1873.19	464	1227.41

* Figure relates to 21 out of 36 Commissionerates

1.13 Fraud/presumptive fraud cases *

The position of fraud/presumptive fraud cases alongwith the action taken by the department against the defaulting assessees during the period 1994-95 to 1996-97 is depicted below:-

(Amount in lakh of rupees)

Year	Cases detected		Demand of duty raised	Penalty imposed		Duty collected	Penalty collected	
	Number	Amount	Amount	Number	Amount	Amount	Number	Amount
1994-95	238	5220.05	4772.59	114	137.07	379.18	95	6.94
1995-96	274	4618.83	3199.56	90	70.67	95.18	66	7.47
1996-97	273	4733.85	3507.61	37	94.71	130.03	18	2.18
Total	785	14572.73	11479.76	241	302.45	604.39	179	16.59

* Figure relates to 21 out of 36 Commissionerates

The above data reveals that while a total of 785 cases of fraud/presumptive fraud were detected during the years 1994-1997 by the department, involving a duty of Rs.145.73 crore, the department raised a demand of Rs.114.80 crore only and recovered Rs.6 crore (5.23 per cent) out of it. Similarly, out of the imposed penalty of Rs.3 crore, the department recovered Rs.0.17 crore only.

1.14 Outstanding audit objections

The number of outstanding audit objections as on 30 September 1997 was 23547 having a duty implication of Rs.3521.67 crore.

The year wise pendency was as under:-

Period upto	Number of objections	Amount in crore of rupees
1992-93	6545	607.61
1993-94	8518	949.91
1994-95	11844	1342.36
1995-96	16679	1955.58
1996-97	23547	3521.67

1.15 Contents of Report

This Report includes 374 paragraphs featured individually or grouped together and two reviews on (i) Modvat credit on capital goods and (ii) soap and detergent, arising from important findings from test check in audit and having a total revenue effect of Rs.3531.78 crore. While the Ministry/department had till November 1997 accepted audit observations included in 192 paragraphs/ reviews involving Rs.53.49 crore, the Ministry did not accept audit observations contained in 10 paragraphs involving Rs.1.86 crore. Reply for the remaining paragraphs/reviews involving Rs.3476.43 crore had not been received (November 1997).

2. MODVAT CREDIT ON CAPITAL GOODS

2.1 Introduction

Modvat scheme was introduced with effect from 1 March 1986 allowing the manufacturer to obtain credit on central excise duties and the countervailing duty paid on specified products. The objective was to mitigate the cascading effect of duties. Modvat scheme was extended to capital goods with effect from 1 March 1994 by introducing a new set of rules in the Central Excise Rules, 1944 in exercise of the powers conferred on the Government under section 37 of the Central Excise Act, 1944. For this purpose rules 57Q to 57U were introduced in Central Excise Rules, 1944 through a notification issued in March 1994.

2.2 Scope of audit

With a view to evaluate the efficacy of the operation of the scheme and its impact on collection of revenue and to examine whether the benefits had been availed in accordance with the provisions of rules, the appraisal of the scheme of 'Modvat credit on capital goods' was conducted during the period from July 1996 to April 1997 covering the records relating to 1994-95 to 1996-97 in respect of 606 manufacturing units in 36 Commissionerates. The findings based on the test check of central excise records are detailed in the succeeding paragraphs.

2.3 Statistical information

Excisable units in existence and the duty paid through PLA and adjustment through RG23A (Modvat credit on input goods), RG23B (Money credit) and RG23C(Modvat credit on capital goods) accounts have been detailed in the following table:-

Year	Total No. of units in existence	Duty paid through PLA	Adjustment of duty through RG23A (Part-II)	Adjustment of duty through RG23B (Part II)	Adjustment of duty through RG23C (Part-II)
			(Amount in crore of rupees)		
1994-95	79439	37208	18251.13	74.77	767.71
1995-96	84940	40009	23918.40	68.44	1672.33
1996-97	N.A	44818	26896.60	133.18	1987.25

*Data compiled by audit from information supplied by the department

The units selected for audit and the duty adjustment through RG23C (Modvat credit on capital goods) accounts has been shown in the following table:-:

(Amount in crore of rupees)

Year	Units selected for audit	Adjustment of duty through RG23C (Part-II)
1994-95	466	304.76
1995-96	606	651.77
1996-97	566	561.24

2.4 Highlights

Test check of records by audit in 36 Commissionerates revealed that in 1051 cases there was incorrect availment of Modvat credit on capital goods to the extent of Rs.249.58 crore. In addition, there was a loss of revenue of Rs.68.47 crore due to non-recovery of interest from 484 assessees for the periods, such funds were lying with them and were incorrectly utilised by them.

⇒ **In 36 Commissionerates, 393 assessees incorrectly availed credit of Rs.66.07 crore on ineligible items. In 233 cases there was also revenue loss of Rs.12.44 crore, by way of interest lost.**

(Paragraph 2.5)

⇒ **In 27 Commissionerates, 112 assessees availed credit of Rs.52.12 crore even before the capital goods were installed or put to use. There was further loss of revenue of Rs.2.26 crore by way of interest in 70 cases.**

(Paragraph 2.6)

⇒ **In 23 Commissionerates, 91 assessees availed credit of Rs.8.27 crore notwithstanding the fact that the capital goods on which the credit was availed were utilised for inadmissible purposes.**

(Paragraph 2.7)

⇒ **In 19 Commissionerates, 68 assessees incorrectly availed Modvat credit of Rs.8.02 crore on capital goods, though the duty element thereon had already been claimed as depreciation under the Income Tax Act.**

(Paragraph 2.8)

⇒ **In one Commissionerate, 2 assessees did not pay duty of Rs.3.12 crore on items manufactured and used within the factory, although no exemption from duty payment was available as the goods were not within the ambit of capital goods.**

(Paragraph 2.9)

⇒ **In 18 Commissionerates, 56 assessees availed Modvat credit of Rs.6.34 crore on capital goods though they were not holding valid duty paying documents.**

(Paragraph 2.10)

⇒ **In 22 Commissionerates, 70 assessees availed Modvat credit of Rs.49.50 crore without filing the requisite declarations or without getting delays in filing such returns condoned.**

(Paragraph 2.11)

⇒ **In 4 Commissionerates, delays in the issue of show cause notices to 10 assessees resulted in loss of revenue of Rs.9.91 crore.**

(Paragraph 2.12)

⇒ **In 16 Commissionerates delay in adjudication of 540 show cause notices issued to 50 assessees involving duty effect of Rs.395.54 crore resulted in financial accomodation being provided to the assessees with consequent loss of revenue of Rs.43.19 crore in the form of interest.**

(Paragraph 2.13)

⇒ **In 20 Commissionerates, 69 assessees did not submit for defacement 22637 duty paying documents involving Modvat credit of Rs.86.47 crore. In the absence of defacement, fraudulent use of the documents could not be ruled out.**

(Paragraph 2.14)

2.5 Credit taken of duty paid on ineligible items

Under rule 57Q(1) of the Rules, credit of specified duty paid on capital goods can be allowed if such capital goods are specified as eligible items. For the purpose of section 'AAAA'- of the Rules dealing with the credit of duty paid on capital goods, as it stood prior to 16 March 1995, 'capital goods' means (a) machines, machinery, plant etc. for producing or processing of any goods or for bringing about any change in any substance for the manufacture of final products, (b) components, spare parts and accessories of the aforesaid machines, machinery etc., and (c) moulds and dies, generating sets and weigh bridges, used in the factory of the manufacturer.

From 16 March 1995, the scope of the above definition had been widened, by adding some more items under clause (d) to rule 57Q, like steam boilers, water gas generators, steam turbine, engines and motors furnace burner, weighing machines, fork lift trucks, lifting equipments, I.C. engines, compressors and electric generating sets etc. used in the factory of the manufacturer.

From 23 July 1996, definition of capital goods was changed by prescribing the items with reference to their headings under the Tariff Act . Accordingly, all machines, machinery, equipments, components, moulds and dies, refractories and refractory materials, tubes and pipes, pollution control equipments etc., specified in rule 57 Q would be treated as capital goods.

The definition of "capital goods" as set out under the rules is restrictive and the words used are that capital goods should be such as are used for production, processing or for bringing about any change in the substance for manufacture of final products. The terminology has been used in the rules viz., 'production', 'processing' or 'for change in

the substance' while defining capital goods would indicate that the capital goods on which Modvat credit could be taken were the ones through which the process and manufacture or change in products are brought out. Production or process would mean physical processing of the goods and the capital goods must have a nexus for bringing about any change in the substance of the goods by direct participation in the manufacturing process.

Test check in audit revealed that credit of duty of Rs.66.07 crore was incorrectly availed on items not covered under the definition of 'capital goods' in 393 cases in 36 Commissionerates. Besides, financial accomodation to the assessees, this also led to non-recovery of interest of Rs.12.44 crore in 233 cases for various periods for which the assessees had utilised the credits. In 68 cases involving duty of Rs.2.10 crore, the department had accepted the objections and had further recovered in 50 of these cases an amount of Rs.1.20 crore and issued show cause notices for Rs.38.14 lakh in 7 cases.

Some of the more important of such cases are given below:

i) Refractory bricks and refractory materials

As per notification No.11/95 CE(NT), dated 16 March 1995, credit of specified duty paid on capital goods falling under chapter 69 shall not be allowed under the provisions of rule 57Q of the Rules, if such goods were received in the factory before 16 March 1995. Similarly, credit of specified duty paid on refractory materials shall not be allowed if such goods were received in the factory before 23 July 1996.

Fifteen assessees engaged in the manufacture of iron and steel and glass products, in eight Commissionerates, incorrectly availed credit of duty of Rs.9.38 crore notwithstanding the fact that the refractory bricks had been received prior to 16 March 1995 and refractory materials (including refractory mortars) were received prior to 23 July 1996. Besides, the utilisation of these credits resulted in a further loss of interest of Rs.1.10 crore in seven cases for the periods between 1 April 1995 and 31 March 1997.

On being pointed out(July 1995/March 1997), the department contended (October 1996) that refractory bricks and mortars being lining materials of furnaces used indirectly in the production of final products qualified for eligibility as capital goods under rule 57Q. The department added that although refractories are specifically included in rule 57Q from 16 March 1995, there was nothing in the Rules to exclude the said goods from the ambit of the said explanation as it stood earlier.

The contention of the department is not tenable since refractory bricks and mortars were specifically included under the definition of capital goods by issue of notification Nos. 11/95 CE(NT) dated 16 March 1995 and 14/96 CE(NT) dated 23 July 1996 respectively. The inclusion of such items specifically in rule 57Q from a later date indicates that the same were outside the purview of the rule prior to 16 March 1995.

ii) Project imports

Five assessees, in four Commissionerates, manufacturing colour TV sets (chapter 85), iron and steel products (chapter 73), carbon black (chapter 28) and glazed tiles (chapter 69) were allowed to avail credit on CVD on project imports items falling under heading 98.01 of the Customs Tariff Act. Since the heading 98.01 was not included in the Central Excise Tariff Act, 1985, the Modvat credit of 1.84 crore of countervailing duty during the periods between April 1994 and March 1996 that was availed on such project items was not in order. The incorrect allowance of Modvat credit had further led to a loss of interest of Rs.31.56 lakh in 3 cases where the credit had also been utilised.

On being pointed out (October 1996/March 1997), the department in one case contended (January 1997) that Modvat credit was allowed on the basis of duty paying documents where CVD under heading 98.01 was mentioned and the department had no other alternative but to allow credit on such duty paid. They added that a show cause cum demand notice was under issue.

The department's contention is not tenable since heading 98.01 was not included in the Central Excise Tariff Act, 1985 and as such the item could not be regarded as specified item under rule 57Q. Moreover, this anomaly was removed by specific insertion

of heading for countervailing duty in rule 57Q by notification dated 1 March 1997 wherein only 75 percent of duty paid on such imported project items was allowed as Modvat credit under the Rules. This corroborated the audit view that such goods falling under heading 98.01 of the Customs Tariff Act were outside the purview of capital goods under rule 57Q prior to 1 March 1997.

iii) Wires and cables

Wires and cables are not capital goods for the purpose of availing credit of duty. As such, no credit of duty paid thereon as capital goods would be admissible.

Five assessees in Bangalore and Belgaum Commissionerates incorrectly availed Modvat credit amounting to Rs.98.94 lakh on wires and cables.

On being pointed out (October 1996 and March 1997), one of the assessees reversed a credit of Rs.1.38 lakh in April 1997; reply in other cases had not been received (November 1997).

iv) M.S. lancing pipes

As per explanation (1)(g) below rule 57Q, tubes and pipes of iron and steel or copper or aluminium used for conveying inputs on which credit of duty is taken, intermediate goods or final products in the factory, came under the ambit of capital goods with effect from 23 July 1996. M.S. lancing pipes are made of iron and steel used for conveying oxygen (input) to the furnace or otherwise for making hole for discharge of molten metals.

An assessee, in Bhubaneswar Commissionerate, engaged in the manufacture of iron and steel had availed Modvat credit of duty paid on lancing pipes amounting to Rs.29.47 lakh during the period March 1994 to 22 July 1996 although the item was not covered under the Modvat scheme on capital goods. The assessee utilised the credit of Rs.10.24 lakh (Rs.8.66 lakh in June 1995 and Rs.1.58 lakh in July 1996) towards

payment of duty on clearance of final products. This resulted in a further loss of interest of Rs.3.24 lakh.

v) Chemicals

An assessee, in Mumbai II Commissionerate, engaged in the manufacture of goods falling under Chapters 28, 29, 31 and 39 had availed Modvat credit of Rs.14.07 lakh during September to December 1994 on chemicals (chapter 27, 28 and 29), treating them as capital goods. Since these items were consumables, their categorisation as capital goods and availment of credit of duty thereon was clearly not in order.

The department recovered the amount in January 1996 at the instance of audit.

2.6 Credit taken on Capital goods before installation and being put to use

Under rule 57Q read with rule 57S, credit of duty shall be taken only when the capital goods are used by the manufacturer of final products and not merely when such goods are received in the factory as emergence of final products would be possible only when such capital goods enter into production. In the case of newly established units, the Board through its circular dated 26 December 1994, clarified that the declarations under rule 57T were still required to be filed and credit could be taken only after the factory commences production. The instructions would equally hold good in the case of units undertaking new lines of production/expansion as the usage of capital goods is a pre-condition laid down by rule 57Q for availment of credit. Provisions were inserted under sub rule (2) of rule 57Q by the notification dated 1 January 1996 specifically providing that no credit on capital goods received in the factory on or after 1 January 1996 should be taken before their installation or use as certified by the manufacturer/designated officer for the purpose.

The notification issued on 1 January 1996 could be treated as only a clarification because by virtue of the definition of the term 'capital goods' itself, no credit could be taken unless the capital goods were used for producing or processing of any goods.

It is noteworthy that any incorrect credit availed by an assessee cannot be disallowed/recovered after expiry of six months period in view of the time barring provision contained in rule 57U.

Test check of records revealed that 112 assessees in 27 Commissionerates had incorrectly taken Modvat credit of Rs.52.12 crore on capital goods even before the said goods were installed or put to use. The Ministry/department accepted the objection in 15 cases involving credit of Rs.76.23 lakh and reported recovery/adjustment of credit of Rs.40.99 lakh in 11 cases and issue of show cause notices for Rs.34.51 lakh in 3 cases. Besides, due to financial accomodation to the assessees, there was non-recovery/loss of interest of Rs.2.26 crore in 70 cases.

Some illustrative cases are given below:

i) An assessee, in Chandigarh Commissionerate, engaged in the manufacture of soda ash & caustic soda lye (chapter 28) availed credit of duty amounting to Rs.9.79 crore on capital goods received during April 1994 to July 1995 for the construction of a new plant under expansion scheme. Out of the above, a credit of Rs.3.19 crore which was on account of Customs duty was not admissible. The credit was reversed in September 1994. Since the new plant started production only on 18 August 1995, the credit of Rs.6.60 crore taken before the crucial date was not in order.

Of the above, a credit of Rs.3.06 crore was also utilised by the assessee during July 1994 to 18 August 1995 towards payment of excise duty for clearance made from another plant of the same factory. This resulted in loss of interest amounting to Rs.48.60 lakh (April 1995 to August 1995).

ii) Two assessees, in Pune Commissionerate, availed Modvat credit amounting to Rs.5.18 crore on capital goods before installation and use thereof. In one case, credit amounting to Rs.2.66 crore was availed in June 1996, whereas the goods were not installed till March 1997. In the second case, the assessee took credit of Rs.2.52 crore during the period December 1994 to March 1996 (out of which Rs.48.60 lakh was after 1 January 1996), but the capital goods were actually put to use only in November 1996.

iii) Five assessees, in Bangalore Commissionerate, had availed and utilised Modvat credit of Rs.4.67 crore being the specified duty paid on the plant and machinery before these were put to use. This resulted in unintended financial benefit to the assessee to the extent of Rs.4.67 crore and consequential loss of revenue on account of interest of Rs.51.45 lakh at 20 per cent not levied for and upto the period the plant and machinery were put to use.

The department stated (July 1996 and January 1997) that objection would be valid only after 1 January 1996.

The contention of the department is not acceptable as the notification dated 1 January 1996 was of a clarificatory nature only.

iv) Four assessees, in Hyderabad and Guntur Commissionerates, procured capital goods at the time of initial setting up/expansion of the units and took credits of Rs.2.73 crore in RG23C during the period April 1994 and October 1995. The machinery items were, actually installed and commercial production started between September 1994 and November 1995.

On being pointed out (October 1996 and March 1997), the department in one case stated (April 1997) that there was no bar in taking credit as it was not availed before the machinery was actually installed and put to use. In another case it contended (July 1997) that since the credits which were taken before the receipt of Board's instructions, were actually utilised only after commencement of production, there was no irregularity or loss of revenue.

The contention of the department is not acceptable as the credits in these cases were admissible only from the dates of commencement of production, taking credits even at the stage of setting up/expansion of the units was violative of the provisions of rule 57Q and Board's instructions of December 1994.

v) A public sector undertaking, in Shillong Commissionerate, engaged in manufacture of goods falling under chapter 27 availed credit of duty of Rs.1.54 crore

between October 1995 and August 1996 on capital goods acquired for Digboi Refinery modernisation project. Though the capital goods had been installed, neither the trial production nor commercial production in the new project had started till the date of audit (November 1996).Thus, the availment of credit of Rs.1.54 crore on capital goods before such goods entered into production process was not in order.

A show cause notice was issued (December 1996) at the instance of audit in this case. Further progress has not been received (November 1997).

2.7 Availment of credit on capital goods for inadmissible purposes

Modvat credit on capital goods, in terms of clause (a) and (b) of explanation 1 below rule 57 Q (1), enables utilisation of credit on capital goods for producing goods or processing goods or bringing about any change in any substance for the manufacture of final products, in the factory of the manufacturer. If the capital goods are used for purposes other than specified purposes, credit of specified duty paid on them is clearly not admissible.

91 assessees in 23 Commissionerates had availed Modvat credit of duty of Rs.8.27 crore on capital goods, notwithstanding the fact that these were neither used for producing goods, processing goods nor for bringing about any change in any substance for the manufacture of final products. The department accepted the objection in 14 cases involving Modvat credit of Rs.43.02 lakh and reported recovery of Rs.14.68 lakh in 7 cases, besides issue of show-cause notice for Rs.28.42 lakh in two cases. In addition, there was a loss of revenue of Rs.1.64 crore in 66 cases on account of non-charging of interest on the amount of financial accomodation for the periods the assessees had utilised the money.

Some of the important cases are mentioned below:

i) Effluent treatment plant

An assessee, in Coimbatore Commissionerate, engaged in the manufacture of wood pulp, viscose staple fibre, yarn etc., was incorrectly allowed to avail (February and March 1996) credit of specified duty of Rs.13.01 lakh paid on capital goods (components and spares) used for the pollution control purpose.

The department justified the availment stating (June 1997) that goods were used in the factory of manufacture of final products.

The reply of the department is not tenable as the goods in question were components used in relation to pollution control purpose which was not a specified purpose for availment of Modvat credit in terms of rule 57Q.

ii) Micro processing system

An assessee, in Bangalore Commissionerate, manufacturing pagers (sub-heading 85.27) availed Modvat credit of Rs.16.77 lakh being the additional duty paid on a micro processor system which was used in the office for processing the data relating to the specifications etc. of the customers' orders. As these were not used in producing, processing or bringing about any change in any substance for the manufacture of the final products (pagers), the credit availed was inadmissible and led further to a loss of interest of Rs.7.26 lakh.

iii) Pilot plant for testing biological waste water treatment

An assessee, in Mumbai III Commissionerate, engaged in the manufacture of synthetic organic dyestuff, organic chemicals, availed Modvat credit of Rs.7.23 lakh in November 1995 for duty paid on a 'pilot plant for testing biological waste water treatment' installed for studying various factors of biological treatment, which was not used for specified purposes for manufacturing final products .

iv) Ethylene truck loading pump installed at place other than factory premises

An assessee, in Pune Commissionerate, engaged in the manufacture of PVC resins availed Modvat credit of Rs.6.64 lakh in April 1996 on "ethylene truck loading pump" not installed within factory premises but 2.5 kms. away.

Department intimated (February 1997) that a show cause cum demand notice for disallowing the credit had since been issued at the instance of audit.

v) Masonary work

Another assessee, in the same Commissionerate, engaged in the manufacture of goods falling under chapter 34, availed Modvat credit amounting to Rs.4.25 lakh during the period November 1995 to January 1996 on items like cement, M.S. beams, angles, plates, H.R. coils etc. As the capital goods, on which credit of specified duty paid was availed, were not used for specified purposes, the credit availed was incorrect.

2.8 Credit taken on capital goods in addition to depreciation claimed under Income Tax Act

As per sub rule (5) of rule 57R, credit of duty paid on capital goods shall not be allowed, if the manufacturer claims depreciation under section 32 of Income Tax Act, 1961 on that part of the value of the goods which represents duty of excise. Provisions of rule 57T(1) also require that a manufacturer availing credit of specified duty shall file a declaration with the department to the effect that he shall not claim depreciation, under section 32 of Income Tax Act, 1961, on that part of the value of capital goods which represents the amounts of specified duty paid on such capital goods. Sub rule (5) of rule 57U, provides for levy of penalty equivalent to the credit availed, in cases where an assessee takes a credit wrongly on account of wilful misstatement or suppression of facts.

According to commercial practice, machine, machinery and parts thereof may be considered as capital goods only when they are capitalised and shown as such in the financial accounts. This aspect has been clarified by amending rule 57R(5) vide

notification No.14/96CE(NT) dated 23 July 1996 wherein credit of duty paid on goods has to be disallowed if the manufacturer claims duty element as revenue expenditure.

i) Credit of duty on goods on which depreciation also claimed

Test check of records revealed that 39 assessees in 15 Commissionerates were incorrectly allowed credit of Rs.1.38 crore on capital goods, notwithstanding the fact that the duty element thereon, had already been claimed as depreciation under the Income Tax Act, 1961. The department accepted the objections in 10 cases involving credit of Rs.81.09 lakh of which an amount of Rs.13.83 lakh had been recovered in 6 cases.

Some of the important cases are discussed below:

a) An assessee, in Chandigarh Commissionerate, engaged in the manufacture of clinker (sub-heading 2502.10) and cement (sub-heading 2502.29) took credits of Rs.61.39 lakh on various capital goods upto 28 February 1995 and also claimed depreciation on the element of credits taken in the capital goods account. This resulted in availment of double benefit viz., Modvat credit of Rs.61.39 lakh as well as depreciation during the year 1994-95.

The department stated (April 1996) that credits of Rs.3.94 lakh taken on items not used in the plant for production were reversed in February-March 1996. Regarding the balance amount of Rs.57.45 lakh, it was stated that depreciation which was claimed during 1994-95 had also been reduced from the total depreciation claimed by the assessee in the assessment year 1995-96.

The fact remains that as both Modvat and depreciation were claimed during the year 1994-95 (Assessment year 1995-96), the assessee was required to expunge the balance credits of Rs.57.45 lakh.

b) An assessee, in Rajkot Commissionerate, had availed credit of duty of Rs.23.24 lakh in January 1995 on procurement of an oxygen plant. Though the assessee had submitted an undertaking in his declaration filed under rule 57T(1) that no depreciation

would be claimed under the Act on the amount of duty credit of which had been availed in his Modvat account, correlation with his Income Tax assessment showed that the assessee had claimed depreciation on the oxygen plant inclusive of specified duty, contrary to the provision of rules and the declaration. This resulted in incorrect availment of credit of Rs.23.24 lakh. Penalty of Rs.23.24 lakh was also leviable in this case due to wilful suppression/misrepresentation of facts.

ii) **Credit of duty paid on consumable goods charged to revenue expenditure**

29 assessees, in 6 Commissionerates, engaged in the manufacture of different items availed credits under the capital goods scheme on consumables, the total expenditure on which including excise duty was charged to the manufacturing accounts/profit and loss accounts i.e., in revenue account as revenue expenditure. The department should have disallowed the Modvat credits availed of, by the assessees. This resulted in loss of revenue amounting to Rs.6.64 crore during the years 1994-95 to 1996-97.

Some of the individual cases are discussed below:

a) Three assessees, in Chandigarh Commissionerate, engaged in the manufacture of yarn (chapter 52 and 55), availed during the years 1994-95 and 1995-96, credit of Rs.90.09 lakh under the capital goods scheme on consumable goods like rubber cots/pads/aprons, tubes, ring-holders, bushes, needle wires, springs, pins, gears, rollers, etc., treating them as capital goods, though these were not capitalised.

The department, in the case of first assessee, stated (December 1996) that the assessee had taken depreciation of the value and not of the duty. In the case of the other two assessees the department stated (April 1997) that these were capital goods which were used in the manufacture of final products.

The contention of the department is not acceptable. These items were booked under revenue expenditure (consumable stores) in the manufacturing/profit and loss

account and not as capital expenditure. As such, these cannot be termed as capital goods under rule 57Q of the Rules.

b) An assessee, in a Calcutta II Commissionerate, manufacturing cast iron spun pipes (chapter 73) availed credit of Rs.38.78 lakh on fire clay/refractory bricks (chapter 69) during September 1996 but the cost of such items including duty paid on the same was claimed as revenue expenditure in their books of accounts. The availment of entire credit was not proper as per the notification dated 23 July 1996.

2.9 Availment of exemption on goods not within the ambit of capital goods

Green tar dolomite bricks falling under heading 68.07 came within the ambit of capital goods vide notification No.14/96 CE(NT) dated 23 July 1996.

Two assessees, in Bhubaneswar Commissionerate, engaged in the manufacture of 'green tar dolomite' filed declaration under rule 173B for the said product and claimed exemption under notification No.67/95CE dated16 March 1995. The assessees cleared 458 tonne green tar dolomite and unburnt refractory bricks during the period April 1995 and April 1996 for their captive use, without payment of duty amounting to Rs.3.12 crore. As the said goods came under the ambit of capital goods with effect from 23 July 1996 only, the availment of exemption before the critical date was improper.

2.10 Availment of credit without valid duty paying documents

As per rule 57T(3) read with rule 57G(2) of the Rules, credit of duty is admissible only if the inputs/capital goods are received under the cover of valid documents, evidencing payment of duty. With effect from 1 April 1994, Modvat credit can be availed on the basis of duplicate copy (transporter copy) of invoice and duplicate copy of bill of entry. Registered dealers are also authorised to issue excise invoice on the basis of which buyers can take Modvat credit.

Test check of records revealed that 56 assessees in 18 Commissionerates, had availed Modvat credit amounting to Rs.6.34 crore on the basis of invalid documents as abstracted in the following table:-

Sl. No.	Type of document	No. of cases	Amount of credit (in lakh of rupees)
1.	Reconstructed bill of entry	1	211.00
2.	Credit taken on invoices not in the name of the assessees	9	92.67
3.	Credit taken on quadruplicate copy	1	63.73
4.	Credit taken on the basis of consumption certificate	1	41.63
5.	Credit taken on photo copy/xerox copy of duty paying documents	3	30.82
6.	Credit taken on copy of challan	3	9.77
7.	Credit taken on the basis of adjustment entry	3	12.31
8.	Credit taken on original copy of bill of entry	1	1.29
9.	Others	34	170.30
	Total	**56**	**633.52**

The department accepted objections involving duly effect of Rs.52.66 lakh in 10 cases of which a recovery of Rs.45.56 lakh on capital goods was reported in 7 cases.

2.11 Filing of declarations

A. Belated condoning/late filing of declarations

According to rule 57T(1), every manufacturer, intending to take credit of duty paid on capital goods under rule 57Q, shall file a declaration with the Assistant Commissioner within a month of the receipt of capital goods. If any declaration is not filed within the maximum extended period of three months from the date of receipt of capital goods, credit of duty shall not be admissible as there is no provision in the rules for condoning delay beyond three months.

61 cases involving incorrect availment of credits of Rs.7.96 crore on the basis of time barred declarations and belated declarations in respect of which the delays were not condoned by the department were noticed in 17 Commissionerates.

Some of the cases are mentioned below:

i) Late filing of declaration - delay not condoned

a) Four assessees, in Ahmedabad Commissionerate, had received 126 items of capital goods involving duty of Rs.3.46 crore during May 1994 to March 1996, for which declarations were filed after receipt of capital goods. Neither the assessees had sought for condonation of delay in filing the declaration nor such delays were condoned by the Assistant Commissioner. Availment of credit of duty without observing the procedure prescribed in the Rules was therefore, improper.

b) An assessee, in Visakhapatnam Commissionerate, engaged in the manufacture of petroleum products, filed four declarations on different dates during January to April 1996 for availing Modvat credit to the extent of Rs.1.64 crore in respect of the capital goods received in the factory during the period December 1995 to March 1996. As all the above declarations were filed only after the receipt of goods with delays ranging from 4 to 39 days, the assessee in his declarations sought for condonation of delay which was not considered by the department till November 1996. Credits of Rs.43.99 lakh on the said goods were, however, availed of by the assessee during August 1996 and October 1996 on the basis of declarations made by him during January 1996 and February 1996, even in the absence of delays having been condoned, in contravention of the provisions of rule 57T(1) of the Rules.

The department accepted the facts (September 1997).

c) An assessee, in Surat Commissionerate, had received '12 consignments' of capital goods involving duty of Rs.61.23 lakh during October 1994 to July 1996. The required declaration were filed, but only after receipt of capital goods. The condonation for delay in submission was sought only in one case in June 1995. Permission was not granted by

the department in that case till the date of audit (October 1996). The availment of credit without obtaining the condonation orders was not in order.

ii) Belated condonation of late filing of declarations beyond the grace period

a) An assessee, in Pune Commissionerate, engaged in the manufacture of sugar availed Modvat credit of Rs.18.09 lakh on capital goods in August 1995. The declaration was filed after the expiry of three months from the date of receipt of the capital goods. The credit availed was therefore, improper.

b) An assessee, in Nagpur Commissionerate, engaged in manufacture of motor vehicle chassis fitted with engine under sub-heading 8706.20, had received capital goods on 4 May 1995. The declaration along with intimation of receipt of capital goods was actually filed by the assessee on 10 November 1995 and the credit of Rs.18.64 lakh was availed of, on the date of filing of declaration i.e., on 10 November 1995 itself. As the assessee had not filed the declaration within the stipulated period, the credit of Rs.18.64 lakh was not admissible to the assessee.

On being pointed out (September 1996), the department stated (January 1997) that since the assessee availed of credit on capital goods in November 1995 after filing of declaration, the credit availed was correct.

The reply of the department is not tenable as the credit taken was clearly not admissible in this case, the relevant declaration having been filed six months after the receipt of capital goods.

B. Credit of duty on capital goods availed without filing declarations

In terms of rule 57T(2), a manufacturer, intending to take credit of the duty paid on the capital goods under rule 57Q, shall intimate the particulars with full description of the capital goods along with brand name and identification marks or numbers if any, particulars of the invoice or bill of entry as the case may be and any other particulars as

the Commissioner may require, to the jurisdictional Superintendent of Central Excise, on receipt of such capital goods.

30 assessees in 13 Commissionerates availed credit of specified duty of Rs.40.13 crore paid on capital goods without filing valid declarations. Besides, there was loss of interest of Rs.7.93 crore in 8 cases.

Some of the cases are mentioned below:

a) An assessee, in Chandigarh Commissionerate, engaged in the manufacture of "electron guns"(sub-heading 8540.90), availed credit under rule 57Q without intimating the jurisdictional Superintendent, the particulars regarding full description of the capital goods along with brand name and identification marks or numbers, if any and the particulars of invoices and bills of entry. As such, the availment of credits aggregating Rs.19.60 lakh during the years 1994-95 and 1995-96 was improper .

The department accepted (March 1997) the lapse and reported that a case was being booked against the assessee.

b) An assessee, in Ahmedabad Commissionerate, availed Modvat credit on various items of capital goods from March 1994 after filing prescribed declarations. However, when items of similar description (same tariff heading) were received on second or subsequent occasions, no fresh declarations were filed but credit of duty was availed on the strength of the earlier declaration against which supplies had already been received. The assessee availed credit of duty against 109 invoices involving duty of Rs.67.92 lakh between June 1994 and February 1996 on the strength of such earlier declaration. The procedure adopted was not in accordance with the provisions of the Rules.

c) Three other assessees, in Surat Commissionerate, availed Modvat credit of Rs.37.27 lakh from March 1994 to September 1996 on 85 invoices of capital goods on the strength of declarations against which supplies had already been effected and for which no fresh declarations were filed.

C. Non-filing/belated filing of D3 intimations

According to rule 57T(2), every manufacturer intending to take credit of duty paid on capital goods shall intimate the particulars regarding full description of the capital goods along with brand name and identification marks or numbers if any, particulars of invoice or bill of entry etc., to the jurisdictional Superintendent of Central Excise as soon as may be, on receipt of such capital goods. As per trade notice dated 4 April 1994, such intimation was required to be filed in form D3 within 24 hours after the receipt of the goods as prescribed under the Rules.

Two cases of availment of credit of Rs.1.40 crore without filing D-3 declarations were noticed.

One of the cases is mentioned below:

A public sector undertaking, in Hyderabad Commissionerate, availed Modvat credit to the extent of Rs.1.40 crore during August 1994 to March 1995, without filing the D3 intimations, in respect of capital goods received in the factory during July 1996 to November 1996, within the stipulated time. The required intimations were filed with delays ranging from one to 40 days and the credit of duty was availed. There was nothing on record to show that the assessee had obtained the permission of the jurisdictional Assistant Commissioner condoning such delays.

The department accepted the facts (September 1997).

2.12 Loss of revenue due to non-issue and late issue of show cause notices

Rule 57U(1) stipulates that where the credit of specified duty paid on capital goods has been taken on account of error, omission or misconstruction, the proper officer may, within six months from the date of such credit (with effect from 16 March 1995, within six months from the filing of monthly return), serve a show cause notice to the assessee requiring him to show cause as to why such credits should not be disallowed and where such credits had already been utilised, why the amount equivalent to such credit

should not be recovered from the assessee (where credit has been taken on account of wilful misstatement, collusion or suppression of facts on the part of the assessee with a view to evade duty, the period of six months stands extended to five years). In cases, where service of notice is stayed by a Court, the period of such stay shall be excluded from computing the aforesaid period of six months or five years, as the case may be.

Ten cases of loss of revenue of Rs.9.91 crore due to non-issue and late issue of show cause notices were noticed in 4 Commissionerates.

Some of the important cases are mentioned below:

i) Issue of ineffective show cause notices being time barred

An assessee, in Chandigarh Commissionerate, engaged in the manufacture of "digital microwave radios" (heading 85.25) availed credit of Rs.85.54 lakh on the capital goods- "testing equipments" on 1 April 1994. A show cause cum demand notice was issued on 7 October 1994 treating them as unspecified items under rule 57Q. Though the demand for Rs.85.54 lakh was confirmed by the jurisdictional Commissioner, the CEGAT on an appeal by the assessee, set aside the Commissioner's orders on the grounds that the show cause cum demand notice, ab-initio, was time barred as it had not been issued within six months from the date of taking of the credit. The late issue of show cause notices, led to a loss of revenue of Rs.85.54 lakh to the Government.

ii) Loss of revenue due to show cause notices not being issued

In Pune Commissionerate, show cause notices were not issued due to time bar resulting in loss of revenue to the Government amounting to Rs.32.41 lakh in the cases relating to 4 assessees.

One of these assessees was served with show cause notices covering the period from October 1994 onwards disallowing the Modvat credit on certain ineligible items like repair kit, programmable logic controllers, measuring heads etc. The assessee had incorrectly availed Modvat credit amounting to Rs.8.12 lakh on similar items during the

period from March 1994 September 1994 also. Show cause notices were not issued to the assessee for this period. This resulted in loss of revenue amounting to Rs.8.12 lakh to the Government.

iii) Loss of revenue due to non-quantification of the recoverable amount in show cause notices

An assessee, in Allahabad Commissionerate, had incorrectly availed credit of Rs.8.69 crore on ineligible items viz., cement and steel under the scheme during May 1994 to August 1996. It was disallowed by the department and this was also upheld by Commissioner (Appeals). However, as the amount involved had not been quantified by the department in the show cause cum demand notices till date (May 1996), the amount could not be deposited as required under section 35F of the Act, before the assessee had gone in appeal before CEGAT. This resulted in loss of interest to the tune of Rs.1.89 crore to the Government because of the non-deposit of the duty involved.

2.13 Delay in adjudication resulting in loss of revenue

The Public Accounts Committee in its 84th Report (1981-82) had adversely commented upon the inordinate delay in finalisation of adjudication proceedings in demand cases. Accordingly, the Board had issued instructions (January 1983 and March 1986) that demand cases should be adjudicated within a maximum period of six months from the date of issue of show cause cum demand notices and delays beyond that period should be brought to the notice of the Commissioner who would discuss the matter with the adjudicating officers to examine the possibility of their expeditious disposal. The inordinate delays in deciding the cases could lead to a situation where the assessees may derive unintended financial accommodation by utilising the disputed credits since the assessees are not prevented from utilising such credits so long as the demands are not confirmed by the department.

The need for finalising the adjudication proceedings assumes greater importance as under the Act/Rules, provision for levy of interest on Government dues is applicable only after (3 months) of determination of duty (other than cases involving mis-

representation etc. with the objective of evading duty). In the absence of provision for levy of interest from the date of the event occasioning the payment of duty, delays in determination/adjudication leads invariably to loss of revenue. Under Direct Taxes, as interest is levied from the dates when it becomes due, irrespective of the fact when assessments are finalised, Government does not lose the element of interest. Towards this end, in order to safeguard Government's interest, there is a need for a similar provisions under the Act, to levy interest from the dates when duty becomes due.

Test check of records in 16 Commissionerates revealed that 540 show cause cum demand notices involving duty effect of Rs.395.54 crore issued to 50 assessees during the year 1994-95 to 1996-97 were pending adjudication for periods beyond six months. In most of the cases, the assessees had already utilised the amount of credits resulting in unintended financial accomodation to the assessees and loss of interest to the extent of Rs.43.19 crore.

Some of the interesting cases are mentioned below:

i) In Jamshedpur Commissionerate, an assessee had incorrectly availed Modvat credit of Rs.33.18 crore on capital goods during September 1994. While the department issued show cause cum demand notice in October 1994, the case had not been adjudicated till March 1997, resulting in blocking of funds to the extent of Rs.33.18 crore and undue financial accomodation to the assessee to the extent of Rs.12.17 crore in the form of interest at 20 per cent per annum for the period June 1995 to March 1997.

ii) Two assessees, in Mumbai III Commissionerate, were served with fourteen show cause-cum demand notices for Rs.20.67 crore for incorrect availment of Modvat credit on ineligible items like M.S. structures etc. used for erecting sheds, cranes, forklift, electric cables, computers, machinery used for generation of electricity before 16 March 1995, during the period April 1994 to September 1996. These show cause cum demand notices were not adjudicated till March 1997 resulting in financial accomodation to the assessees to the extent of Rs.4.71 crore by way of interest lost besides blocking of Government's revenue of Rs.20.67 crore.

iii) A public sector undertaking in Visakhapatnam Commissionerate, had claimed Modvat credit under rule 57Q, on certain items such as pipes and pipe fittings, electrical apparatus/equipment etc. and availed credit to the extent of Rs.5.63 crore during the period March 1995 to December 1995. The department disputed the admissibility of the credits and issued 17 show cause cum demand notices between January 1995 and April 1996. Despite the fact that written representations were submitted by the assessee in all these cases, the department did not finalise the adjudication proceedings even after delays ranging from 6 to 20 months. It was seen that out of the above disputed Modvat credit, an amount of Rs.2.23 crore was already utilised by the assessee towards payment of duty on final products during the period March 1995 to March 1996. The non-adjudication of show cause notices resulted in unintended financial accomodation involving loss of interest to the extent of Rs.76.36 lakh besides blocking of revenue to the extent of Rs.5.63 crore.

The department, while confirming the facts contended (May 1997) that when it disallowed similar credits for the period prior to 1995, the Commissioner (Appeals) had set aside (1995) the order with a direction to re-examine the eligibility against which the department had gone in further appeal in June 1996 and as such the show cause notices were kept in abeyance, pending decision by CEGAT.

The reply is not tenable as (i) the delays in adjudication relate to the show cause notices issued between January 1995 and April 1996 of which 15 show cause notices issued upto September 1995 became due for finalisation between July 1995 and March 1996 itself, whereas the department filed the appeal only in June 1996; (ii) the adjudication cannot be kept in abeyance on the plea that a case was pending before the Tribunal as non-confirmation of demands involves loss of interest in the event of the case being subsequently decided in favour of the department, since the provisions enable the department to levy interest only after the expiry of 3 months from the date of serving of a demand notice.

2.14 Delay in filing the returns and delay in defacing of the duty paying documents leading to possibilities of fraud

As per rule 57T(6), a manufacturer of the final product shall submit within five days after the close of each month to the Superintendent concerned, the original documents evidencing the payment of duty along with the extracts of part I and II of RG-23C every month and the Superintendent shall, after verifying their genuineness, deface such documents and return the same to the manufacturer.

Test check of records revealed that 69 assessees in 20 Commissionerates did not submit 22,637 duty paying documents involving Modvat credit of Rs.86.47 crore to range officers for defacement. The department also did not demand these documents. Due to non-submission of these documents, the defacement was not done. In the absence of the defacement of these documents, possibilities exists for the fraudulent misuse of these invoices towards utilisation of Modvat credit.

Mumbai III Commissionerate headed the list of duty paying documents not submitted with the number of documents being (4881) followed by Belgaum (4410), Rajkot (3480), Vadodara (2479), Surat (1549), Bangalore (1681) and Ahmedabad (1026). Rajkot Commissionerate headed the list in respect of the amount of duty involved (Rs.2027.06 lakh) followed by Belgaum (1835.44 lakh), Mumbai (Rs.1568.22 lakh), Vadodara (866.61 lakh) and Jamshedpur (Rs.690.70 lakh).

2.15 Credit taken on inadmissible duties

In terms of explanation (2) to sub rule (1) of rule 57 Q, specified duty for the purpose of availment of credit on capital goods shall mean (i) duty of excise levied under the Central Excise Act, 1944 and (ii) Additional duty (countervailing duty) levied under section 3 of Customs Tariff Act, 1975.

Test check of records revealed that 27 assessees in 17 Commissionerates had taken Modvat credit of customs duty, additional duty on textiles, credit of assessable value or of duty paid in excess to the extent of Rs.86.98 lakh, notwithstanding the fact

that these were not the specified duties for which Modvat credit was admissible. Department accepted irregularities in 10 cases involving duty of Rs.19.62 lakh of which Rs.13.26 lakh were recovered in 8 cases.

Some cases are mentioned below:

i) Credit taken of customs duty

Two manufacturers of cold rolled sheets and of telephone cables, in Chandigarh and Hyderabad Commissionerates, incorrectly availed Modvat credit of basic customs duty amounting to Rs.6.75 lakh paid on imported capital goods, despite the fact that basic customs duty levied on imported goods is not covered for availment of credit under the relevant provisions of the Rules.

Department reported (January 1997) that the credit of Rs.6.75 lakh wrongly taken and utilised was debited by the assessees in RG 23A Part II account in August 1996.

ii) Credit taken of assessable value

A manufacturer of steel, in Bhubaneswar Commissionerate, had availed credit of both assessable value and CVD of Rs.2.51 lakh (Rs.2.26 lakh+Rs.0.25 lakh) paid on capital goods. This resulted in excess and incorrect availment of credit of Rs.2.26 lakh.

The assessee has since reversed the amount of Rs.2.26 lakh at the instance of audit.

iii) Availment of credit of duty paid in excess

The term 'specified duty' as explained in the explanation (2) below rule 57 Q (i) covers only duty of excise and additional duty (viz., CVD) levied under section 3 of Customs Tariff Act, 1975. Therefore, credit cannot be granted to any other duty paid and duty paid in excess of what is required to be paid.

a) An assessee, in Jaipur Commissionerate, engaged in the manufacture of grey portland cement, falling under sub-heading 2502.29 imported a "roller" from Hamburg

(Germany) and classified it under sub-heading 8474.90 as spare part of the machinery although the roller has its individual function and was covered under machinery (heading 84.74) as per HSN explanatory note at page 1307. The assessee had paid and claimed Modvat credit of CVD at the rate of 15 per cent - as spare part instead of at the applicable rate on machine at the rate of 10 per cent ad valorem. This resulted in excess availment of credit of Rs.17.08 lakh during June 1996.

b) A manufacturer of cement, in Raipur Commissionerate, imported two diesel generating sets as capital goods and availed credit of countervailing duty paid at the rate of 15 percent ad valorem classifying the goods under heading 85.03. The goods in question were D.G. sets and were correctly classifiable under heading 85.02 only, attracting duty at the rate of 10 per cent ad valorem. Due to incorrect classification of D.G. sets, CVD was paid more than the effective rate applicable and resulted in availment of Modvat credit of Rs.13.87 lakh in excess.

On being pointed out (March 1997), the department stated (May 1997) that the Commissioner of Customs, Mumbai has been requested to re-examine the classification of the goods at his end.

iv) Duty paid on own volition

According to clarification issued by the Board on 4 January 1991, the assessee does not have the option to pay duty on his own volition in case the goods are exempted from whole of duty of excise leviable, thereon. Machines, machinery manufactured and used captively within the factory of production after 16 March 1995 were exempted from duty. In case the assessee pays duty on such exempted goods, it will not be treated as duty but as deposit with Government and equivalent credit availed thereof was required to be reversed.

Two assessees, in Aurangabad and Pune Commissionerates, paid duty on the capital goods manufactured and consumed captively after 16 March 1995 and availed credit of the same, amounting to Rs.5. lakh. As the duty paid on exempted goods cannot be treated as duty of excise, availment of credit was incorrect.

2.16 Availment of credit of specified duty paid on capital goods used for manufacture of unspecified final products

Rule 57Q as substituted with effect from 16 March 1995 stipulates grant of credit of specified duty paid on capital goods when used for the purpose of manufacturing specified final products. Annexure to rule 57Q excludes (i) all goods falling under chapter 24; heading 36.05; 37.06; and (iii) all woven fabrics falling under chapter 52 or 54 or 55. These goods were, therefore, unspecified final products for which Modvat credit on related capital goods was not admissible.

7 assessees in Chennai, Cochin, and Vadodara Commissionerates, engaged in the manufacture of cotton yarn, cotton fabrics, man made fabrics and caprolactum, falling under chapter 52, 54, 55 and 29 respectively of the Tariff, were allowed to take Modvat credit of Rs.1.12 crore of duty paid on capital goods from March 1995 to January 1996, which were used for final products, not specified under rule 57Q. Accordingly, the assessees were not eligible for availing Modvat credit on the machines used for producing woven fabrics.

Department, in the case of Chennai Commissionerate stated (June 1996) that the machinery such as warp beam and warp beam flanges were used for winding yarn at the warping stage and the warped yarn was cleared on payment of duty for captive consumption.

The contention of the department is not acceptable since the unit being a composite mill, the capital goods installed in the mill were used for the finished product which was specifically excluded from the purview of rule 57Q, ibid. Reply in the other two cases was awaited (November 1997).

2.17 Loss to the Government due to absence of suitable provisions in the Rules

As per rule 57R(1), credit of the specified duty paid on capital goods shall not be allowed if such capital goods are used exclusively for final products which are exempt from whole of the duty of excise leviable thereon (other than a final product which is

exempt from the whole of the duty of excise leviable thereon under any notification where exemption is granted based upon the value or quantity of clearances made in a financial year) or is chargeable to nil rate of duty. In case, capital goods are used for manufacture of both excisable as well as non-excisable (exempted) goods, the absence of a suitable provision in rule 57R similar to rule 57CC, prescribing for reversal of pro-rata credit of duty paid on capital goods used for manufacture of exempted goods, results invariably in unintended benefit to the assessees. Towards this end, there is need to incorporate a provision in the Rules for reversing Modvat credit on capital goods on a pro-rata basis when these are used both for dutiable and exempted goods. Test check of records revealed excess availment of credits of Rs.18.42 crore in 22 cases.

Some of the important cases are mentioned below:

i) Credit used for clearance of duty free goods

Six assessees, in six Commissionerates, manufacturing cotton yarn, tractors, woollen goods, pig iron-foundry grade, sand moulds, table cover, table inset etc. took Modvat credit of Rs.8.48 crore on capital goods during the year 1995-96. The manufacturers produced and cleared exclusively duty free finished goods. Since no dutiable goods were manufactured and cleared during the year 1993-94, 1994-95 and 1995-96, the Modvat credit of Rs.8.48 crore taken on capital goods was clearly not admissible.

ii) Credit utilised for manufacture of both excisable and non-excisable goods

13 assessees, in 13 Commissionerates, availed Modvat credit of Rs.13.74 crore on capital goods during 1994-95 and 1995-96 which were used for manufacture and clearance of both excisable as well as non-excisable goods. The percentage of dutiable and non-dutiable goods ranged between 24.78 and 83.28, respectively. Utilisation of entire credit on capital goods against clearance of excisable and non-excisable goods could not be checked in the absence of a restrictive clause under rule 57R, similar to rule 57CC relating to input goods. As such the manufacturers utilised the entire amount of Modvat credit inspite of the fact that capital goods were used for manufacture of only

24.72 per cent (on an average) excisable goods. Based on this, Modvat credit of Rs.9.94 crore should have been reversed but could not be reversed, in absence of suitable provisions in the Act/Rules.

2.18 Incorrect availment of credit of duty on removal of capital goods to job workers

According to rule 57S(6), a manufacturer may with the permission of the Commissioner of Central Excise and subject to such terms and conditions as he may impose, remove the moulds and dies to a job worker without payment of duty for the purpose of production of goods on his behalf. However, this is subject to the condition that the goods so manufactured and moulds and dies are returned to the manufacturer within a period of three months or the extended period as may be permitted by the Commissioner. According to rule 57T(3), no credit of specified duty shall be taken unless such capital goods have been received in the factory premises of the manufacturer under the cover of valid duty paying documents.

Two cases of incorrect availment of Modvat credit on capital goods noticed in audit are mentioned below:

i) An assessee, engaged in the manufacture of washing machines in Trichy Commissionerate, was allowed to clear moulds and dies without payment of duty to another manufacturer, who was not a job worker but an independent manufacturer. Duty was required to be paid by the assessee as per rule 57S. The adoption of incorrect procedure viz., clearance of moulds to other than job workers resulted in non-payment of duty of Rs.23.70 lakh during June to July 1996.

On being pointed out (August 1996), the department admitted the objection and stated (December 1996) that a show cause cum demand notice demanding duty of Rs.23.70 lakh had since been issued.

ii) Another assessee, in Mumbai III Commissionerate, availed Modvat credit amounting to Rs.9.36 lakh during April 1996 to August 1996 on moulds and dies which

were not received back in the factory. The moulds and dies were directly sent to job worker's premises by the supplier. The job worker did not return the moulds and dies to the manufacturer within the stipulated period. Availment of credit without the receipt of capital goods in the factory was not in order.

2.19 Removal of capital goods as waste and scrap without payment of duty

Under proviso to rule 57S(1)(ii) of the Rules, read with notification No. 23/94-CE(NT) dated 20 May 1994, capital goods without being used in or in relation to the manufacture of final products may be removed from the factory for home consumption on payment of duty of excise, provided that such duty of excise shall in no case be less than the amount of credit that has been allowed in respect of such capital goods under the relevant rule. If the capital goods are sold as waste and scrap, duty leviable shall be at the rate applicable to such waste and scrap at the time of clearance/sale of such goods.

Three assessees, in three Commissionerates, after availing Modvat credits of duty paid on capital goods did not pay duty of Rs.7.51 lakh on clearance of such goods as scrap. Department reported recovery of Rs.0.30 lakh in one case at the instance of audit.

A case is mentioned below:

A public sector undertaking, manufacturing iron and steel products (chapter 72 and 73 etc.) under Bolpur Commissionerate, availed credit of duty paid on refractory bricks and aluminium silicate bricks (heading 69.07) towards payment of duty on final products. The assessee, after availing of the credit, cleared 500890 pieces of rejected bricks during 1995-96 without payment of duty. This resulted in non-levy of duty of Rs.5.60 lakh during 1995-96.

2.20 Cases of procedural irregularities

i) Availment of duty paid on input goods as duty paid on capital goods

The CEGAT, in the case of Collector of Central Excise Vs. Durgapur Cement Works {1997 (90) ELT 197 (T)}, has held that steel balls used in cement grinding mills

as grinding media, are essential for the grinding process. Although grinding media is not a raw material, it is consumed to some extent in the final product. Accordingly, grinding media is eligible for credit under rule 57A (Modvat credit on input goods) of the Rules.

Test check of records of 2 assessees, in 2 Commissionerates, revealed that the assessees took credit of specified duty amounting to Rs.1.04 crore on input goods as credit of specified duty paid on capital goods. A case is mentioned below:

An assessee, in Chandigarh Commissionerate, engaged in the manufacture of cement (sub-heading 2502.29), was allowed to avail credits on "grinding media/grinding balls" (heading 73.25) under capital goods notified under rule 57Q. Since, these were consumable goods which were also charged to raw material/profit and loss account as revenue expenditure, the credits were correctly available under rule 57A, ibid. This resulted in incorrect availment of credits amounting to Rs.1.03 crore during April 1994 to March 1997.

ii) Utilisation of Modvat credit on capital goods incorrectly for unspecified purposes

Under the provisions of rule 57S(2), credit of specified duty allowed in respect of capital goods may be utilised towards payment of duty of excise on (i) any final products manufactured in the factory of the manufacturer, (ii) on the waste, if any arising in the course of manufacture of the final products and (iii) on the capital goods themselves if such capital goods are removed.

Accordingly, credit of duty paid on capital goods cannot be permitted to be used for any purpose, other than those mentioned above.

26 assessees, in 14 Commissionerates, took credit of Rs.1.63 crore and utilised it for payment of duty, in contravention of provisions of rule 57S(2). In ten cases involving duty of Rs.42.37 lakh the objections were accepted and Rs.40.48 lakh recovered.

A few illustrative cases are mentioned below:

a) An assessee, in Aurangabad Commissionerate, engaged in the manufacture of seamless tubes, falling under chapter 73, utilised the credit amounting to Rs.16.06 lakh on capital goods for payment of confirmed demands of earlier period relating to Modvat credit availed on ineligible inputs and on rejected raw material returned, which was improper.

The assessee debited an amount of Rs.16.06 lakh in PLA in September 1996 at the instance of audit.

b) An assessee, in Chandigarh Commissionerate, took Modvat credit of Rs.2.05 crore on capital goods for the first time during February 1995. Out of above, a sum of Rs.42.19 lakh on account of differential duty pertaining to the period March 1994 to December 1994 was paid by debiting in RG23C part II during June 1995. The differential duty was required to be paid through PLA. This also resulted in undue financial accommodation by way of interest amounting to Rs.6.33 lakh on improper utilisation of credit for the period July 1995 to March 1996.

The department, contended (May 1997) that at other occasion the assessee had paid duty of Rs.74.71 lakh through PLA during March 1996 though sufficient balances were available in RG23A and RG23C.

The reply of the department is neither relevant nor tenable as utilisation of Modvat credit in RG23C towards payment of differential duty was prohibited in terms of the relevant rules.

c) An assessee, in Vadodara Commissionerate, manufacturing excisable goods falling under chapters 15, 29 and 34 debited his RG23C account with Rs.24 lakh being the Modvat credit availed on inputs. Debiting the account (RG23C) of Modvat credit on capital goods, between January 1996 and September 1996, instead of RG23A account was contrary to the provisions of the Rules.

iii) Duty not paid on self manufactured capital goods

With effect from 16 March 1995, capital goods manufactured in a factory and captively consumed for the manufacture of finished excisable goods are exempted from payment of duty vide notification No.67/95 CE dated 16 March 1995. But prior to 16 March 1995, the manufacturer of capital goods clearing the goods within the factory of production, had to pay duty on such manufactured capital goods and in turn utilise the credit thereof towards payment of duty on the final products. There was no exemption on this account.

During the period prior to 16 March 1995, 18 assessees in 9 Commissionerates manufactured and consumed captively machineries without payment of duty amounting to Rs.22.41 crore. Department accepted 4 cases with duty effect of Rs.17.27 lakh and recovered the duty amounting to Rs.14.00 lakh in three cases besides issue of show cause cum demand notice for Rs.3.27 lakh in one case.

Some illustrative cases are mentioned below:

a) An assessee, in Bhubaneswar Commissionerate, manufactured carbon electrodes (anode assembly) by procuring raw materials like C.P. coke and CT pitch during the period June 1994 to February 1995 and captively consumed 20313 tonne of CP coke and 9793 tonne of C.T. pitch for manufacture of carbon electrodes. The assessee neither filed a declaration under rule 173B nor paid duty towards clearance of the carbon electrodes for its captive consumption. The total duty involved on this account relating to the period June 1994 to February 1995 worked out to Rs.5.05 crore.

b) Another assessee, in the same Commissionerate, manufactured Iron and Steel under chapter 72 and 73 and cleared ingot moulds towards captive consumption during the period July 1994 to March 1995 without payment of duty amounting to Rs.2.06 crore, contrary to the provisions of the Rules.

c) An assessee, in Allahabad Commissionerate, engaged in the manufacture of iron and steel products manufactured and consumed captively, excisable goods prior to 16 March 1995 without payment of duty of Rs.11.73 crore, though required to do so under the Rules.

iv) Transfer of unutilised credit balances due to shifting of site, amalgamation of units etc.

As per rule 57S(4) read with notification No. 34/95(NT) dated 16 August 1995, the Commissioner of Central Excise may on an application made by a manufacturer and subject to such conditions and limitations as he may impose, permit a manufacturer having credit in his account in form RG23C maintained under rule 57T and lying unutilised on account of change in ownership or change in site of a factory, resulting from sale, merger, amalgamation or transfer to joint venture with the explicit provision for transfer of liabilities of the old factory, to transfer such unutilised credit to such sold, merged, amalgamated or transferred factory.

An assessee - a limited company, in Bolpur Commissionerate, manufacturing goods (chapter 85 and 38) was renamed as a joint venture company with effect from 1 January 1996. The assessee had a credit balance of Rs.32.34 lakh in its RG23C part-II account as on 1 January 1996 which was transferred to the RG23C part-II account of the new company and partly utilised subsequently. However, no permission to transfer the credit though required under the Rules was taken, resulting in improper availment of Modvat credit for Rs.32.24 lakh during the year 1995-96, besides a loss of interest for Rs.1.61 lakh during October 1996 to December 1996.

On being pointed out (November 1996), the department contended (December 1996) that obtaining of permission was only a technical requirement and its violation was not a substantive violation.

This contention of the department is not tenable as a statutory provision was incorporated in rule 57S of the Rules, for obtaining permission from the jurisdictional Commissioner which was not observed in the instant case.

The above points were brought to the notice of the Ministry in September 1997; their reply has not been received (November 1997).

3. SOAP AND DETERGENT

3.1 Introduction

While soaps are essentially oil based salts of fats, mostly saturated ones, detergents are materials having cleaning action as soap (all soaps are detergents but not vice-versa) and usually refer to synthetic chemicals (or soapless soaps) and are characterised by the presence of "organic surface active agents" (OSAA). Soaps and detergents have been classified under heading 34.01 of the schedule to the Central Excise Tariff Act, 1985.

3.2 Revenue trend

The year-wise contribution of soap and detergents to central excise revenue was as under:

Year	Soap	Detergent
	(Amount in crore of rupees)	
1992-93	186.34	164.05
1993-94	253.82	285.40
1994-95	310.82	206.10
1995-96	335.97	254.41
1996-97	414.20	236.72

3.3 Scope of audit

Records/documents relating to the assessment, levy and collection of duty on soap and detergent relating to the three-years period 1994-95 to 1996-97 in respect of 156 units (59 per cent of the total 264 units) were test checked in audit during July 1996 to March 1997.

3.4 Highlights

There was escapement/short levy of duty aggregating Rs.121.75 crore on 'soap and detergent'. Some of the important findings are as follows:

⇒ **Due to lacuna in the existing Act/Rules, certain major manufacturers/brand name owners were able to get their products manufactured and cleared by other manufacturers (job workers) at an agreed price which was much lower than the prices of their own similar products or the prices at which these goods were finally cleared in the wholesale market through their depots, thereby depriving Government of Rs.68.25 crore in the form of revenue. Accordingly, there is a need to shift the basis for levy of duty on 'soaps' in terms of maximum retail price at which these are sold, under the new section 4A of the Act.**

(Paragraph 3.5(i))

⇒ **Consequent to the introduction of invoice based assessments, manufacturers of products have been making reduction in the assessable value without justification. Since such reductions are not subject to any checks by the department, this resulted in Government being deprived of a revenue of Rs.7.55 crore.**

(Paragraph 3.5(ii))

⇒ **Acceptance by the department of incorrect classification of products like 'preparations for use on hair' and 'dish wash bars' etc. by the manufacturers resulted in Rs.6.03 crore of excise duty not being levied.**

{Paragraph 3.6(i) & (ii)}

⇒ **Despite the restriction imposed by the Drug Controller (India) on marketing of soaps having a 'total fatty matter' content of less than 60 per cent as 'toilet soaps', the department allowed beauty/bathing bars with less than the required percentage of TFM to be cleared as 'toilet soap'. Such products need to be classified separately in line with the instructions of the Drug Controller (India).**

{Paragraph 3.6 (iii)}

⇒ **Ten manufacturers were able to evade duty of Rs.3.66 crore by suppressing their production.**

(Paragraph 3.7)

⇒ **Certain big manufactures by getting their branded goods manufactured through KVIC units were able to clear the same without payment of duty by getting the benefit of exemption meant for KVIC units. In one such case alone, the revenue loss to the Government was Rs.2.45 crore.**

{Paragraph 3.8 (i)}

⇒ **Departmental inaction in recovering confirmed demands, issue of delayed 'show cause notices' after the limits of time-bar and delays in adjudications and finalisation of provisional assessments etc. resulted in non-recovery of duty of Rs.43 crore and further loss of Rs.19.79 crore by way of interest.**

(Paragraph 3.9)

3.5 Valuation

According to section 4 of the Act, where goods are assessable on ad valorem basis, the normal price, is the price at which such goods are ordinarily sold by the assessee to a buyer in the course of wholesale trade, for delivery at the time and place of removal and where the buyer is not a related person and the price is the sole consideration for sale. Supreme Court in the case of Union of India versus Bombay Tyre International {1983 (14) ELT (1896)} have held that value of an article for purpose of levy of excise duty shall include all costs and expenses which have given the article its marketability.

Government, by a notification issued on 1 March 1994 (effective from 1 April 1994), introduced a system of assessment based on the invoice value for all excisable goods. Under this system, the invoice of the assessee serves as `transport document' as well as the basis for determining the `assessable value' under the Act/Rules. The value of goods in such cases is to be determined in accordance with the provisions contained in section 4 of the Act read with the Valuation Rules.

In 23 Commissionerates, 56 cases of undervaluation of excisable goods involving duty effect of Rs.80.37 crore were noticed during test check of records.

i) Branded goods manufactured by others - avoidance of duty

The modus operandi of avoiding duty and thereby causing loss to the Government revenue is as follows:

i) The brand name owner (major manufacturer) although gets his goods (soaps and detergents) manufactured from other manufacturers (the so called job workers) but shows these transactions as purchases from unrelated manufacturers on principal to principal basis on an agreed price which is substantially lower than the comparable assessable value of similar/same products manufactured by the brand name owner himself. Duty is however, paid at the agreed price which is much lower than the wholesale price at which similar products of the brand name owner are cleared. The final products manufactured by the brand name owner and those manufactured through the job worker are indistinguishable and are sold at the same 'maximum retail price' and under the brand name of the owner company.

ii) The brand name owner gets the products manufactured through others on the so called principal to principal basis at an agreed price. Duty is paid by the job worker on such agreed price. The goods are however, cleared in the wholesale market by the brand name owner only and at a much higher price. There being no wholesale transactions at the factory gate of the job workers, the price charged by the brand name owner in the wholesale trade should have been the basis of levying central excise duty.

The existing provisions in the Act/Rules etc., do not prohibit or check such avoidance of duty. Accordingly, Audit is of the view that there is a need to levy the duty on soaps on the basis of 'maximum retail price' and this could be done by the Government by resorting to the new section 4A of the Act, as has since been done in the case of detergents.

In 12 Commissionerates, test check of records in audit showed that the Government had to forego revenue of Rs.68.25 crore due to payment of duty on lesser value by adopting the aforesaid techniques. Of these, avoidance of duty in five cases alone, by accepting the prices at which the job workers cleared the goods to the brand name owners for sale in the wholesale market, amounted to Rs.50.44 crore.

ii) Arbitrary lowering of the assessable value under the invoice based system

Prior to the introduction of `invoice based system' from 1 April 1994, the manufacturer of excisable goods had to get the prices approved (by way of price list). Any subsequent reductions in these prices were also required to be approved by the Assistant Commissioner with justification, before these goods were cleared at lower prices. However, subsequent to the introduction of invoice based system, no such approval was required and the manufacturer could clear the goods at the lower price by just indicating it on the invoice and pay the reduced duty, though the 'maximum retail prices' of the products may be showing a rising trend. Under the new system, the department does not have any formalised mechanism to check whether such price reduction/lower prices were genuine.

In 7 Commissionerates, test check of records revealed that in 12 cases, arbitrary reduction of assessable value had resulted in duty of Rs.7.55 crore being short paid.

Two such cases are illustrated below:

a) A manufacturer, in Indore Commissionerate, entered into an agreement with the buyer who was also owner of the brand name for manufacture of detergent powder as per latter's specifications and entire production was sold to the buyer. Though the transactions were said to be on principal to principal basis, the manufacturer had received a sum of Rs.12.80 crore from the buyer and simultaneously assessable value of goods was reduced by the manufacturer from 1 April 1994 (viz., from the date invoice based assessment system was introduced) without assigning any reason despite the fact that selling price (maximum retail price) of the goods had remained the same or was on higher side. Based on the price prevailing as on 31 March 1994 and the price reduced from 1

April 1994, there was a short realisation of duty amounted to Rs.4.12 crore in respect of clearances made between 1 April 1994 and 30 June 1996.

b) Another assessee, in Chandigarh Commissionerate, was manufacturing a branded detergent powder for the principal manufacturer on payment of duty as per price list. The assessable value was reduced arbitrarily without furnishing any justification with effect from 1 April 1994, on introduction of invoice based system of assessments, resulting in short levy of duty of Rs.2.34 crore during April 1994 to February 1996.

The department did not admit the objection and stated (May 1997) that the assessee had declared the assessable value on 'cost construction method' on the basis of Supreme Court's judgement in the case of M/s Ujagar Prints V/s Union of India {1989 (39) ELT 493 (SC)}. The reply of the department is not tenable as the value on the basis of cost construction method was to be adopted only where value of comparable goods was not known, which was not the issue in the instant case. This view had also been confirmed by the Board itself through its instructions dated 21 March 1994.

iii) Additional consideration not accounted for

Where price is not the sole consideration, the assessable value of the goods, as per the provisions of rule 5 of the Valuation Rules, shall be based on the aggregate of the price and money value of additional considerations flowing directly or indirectly from the buyer to the assessee.

In 11 Commissionerates, 13 cases of short levy of duty of Rs.2.33 crore due to undervaluation of goods on account of non-inclusion of items of expenditure like quantity discount not passed on to the buyer etc., where price charged was not the sole consideration for sale, were noticed.

iv) Incorrect valuation

In six Commissionerates, test check in audit revealed short levy of duty of Rs.1.36 crore in 10 cases due to incorrect computation of assessable value by not including the cost elements like landed cost, royalty paid, overhead expenses etc.

3.6. Evasion of duty by classifying items incorrectly

In 10 Commissionerates, test check of records revealed incorrect classification of the goods involving duty effect of Rs.6.03 crore in 19 cases. Of these, in two cases the department accepted objections involving duty effect of Rs.3.77 crore.

A few such cases are illustrated below:

i) Detergents

In terms of note 2 to chapter 34, "soap" under heading 34.01 applies only to soap soluble in water. Soap and other products of heading 34.01 may contain added substances (for example disinfectants, abrasive powders, fillers or medicaments). Product containing abrasive powders are classified under heading 34.01 only if they are in the form of bars, cakes or moulded pieces or shapes. In other forms, they are to be classified under heading 34.05 as "scouring powders and similar preparations".

Two assessees, in Madurai and Trichy Commissionerates, manufactured and cleared "dish wash bar" after getting it classified under sub-heading 3405.40 liable to duty at 20 per cent ad valorem. Detergent cakes contained 'feldspar' (an abrasive material) in addition to the other ingredients.

The classification of 'dish wash bar' under heading 3405.40 was confirmed by the jurisdictional Assistant. Commissioner vide orders in original dated 31 May 1996 after adjudicating show cause notice in respect of one assessee in Madurai Commissionerate.

Audit pointed out that the classification of detergent cakes under sub-heading 3405.40 was not correct because the product merited classification under sub-heading

3401.20 attracting duty at 30 per cent ad valorem in terms of chapter Note 2 and HSN explanatory notes (page 402) under chapter 34, as it contained abrasive powder and that the incorrect classification had resulted in short levy of duty of Rs.3.67 crore during April 1993 to February 1997.

The department reported (May 1997) issue of SCN for Rs.52.85 lakh covering clearances for the period October 1996 to February 1997. Report for the earlier period has not been received (November 1997).

ii) Preparation for use on hair

Preparation for use on hair are classifiable under sub-heading 3305.90 of the Tariff, attracting duty at 50 per cent and 40 per cent ad valorem, from April 1994 and 16 March 1995, respectively. Tribunal in the case of M/S Henna Export Corporation Vs. Collector {1993(67)ELT-907(T)} held that 'Herbal Shikakai Powder' sold in unit packing with labels indicating its use for the hair was classifiable under heading 33.05.

a) An assessee, in Ahmedabad Commissionerate, manufactured "shikakai soap" and cleared the product on payment of duty at 20 per cent ad valorem after getting it classified as toilet soap under sub-heading 3401.10 (now 3401.19). As printed wrapper of the product indicated that the product was meant for use on hair as 'beauty soap' for the hair and hence meant for conditioning/beautifying the hair, it merited classification under heading 33.05. The incorrect classification resulted in short levy of duty of Rs.85.94 lakh during April 1994 to September 1996.

b) Similarly, another assessee, in Chandigarh Commissionerate, manufactured 'shikakai soap noodles' on job work basis and cleared the goods as toilet soap (heading 34.01) to the brand name owner or his job working units, for further use in the manufacture of 'shikakai soap' from April 1994 onwards, on payment of duty at 20 per cent ad valorem. The printed wrapper of the final product indicated that the product was meant for use on hair as 'beauty soap for the hair'. Thus 'shikakai soap noodles' exclusively used in the manufacture of 'shikakai beauty soap' for hair merited

classification under sub-heading 3305.90. Incorrect classification had resulted in short levy of duty of Rs.79.16 lakh during May 1994 to December 1996.

The department contended (May 1997) that the assessee had only manufactured soap noodles (an intermediate product) which was then further used in the manufacture of 'shikakai soap'. Therefore, noodles cannot be termed as preparation for use on hair and were rightly classified under heading 34.01.

Contention of the department is not tenable because soap noodles not having been classified distinctively under the Tariff merit classification as per classification of final product in which these noodles are used, in terms of rule 2 (a) of the Rules for the Interpretation of the Tariff Act.

iii) Bathing/Beauty bars –need for distinct classification

The Drugs Controller (India), Director General Health Services, New Delhi in his circular dated 15 April 1993 directed all the state drugs controllers that the soap manufacturers be asked to strictly follow the 'Bureau of Indian Standards'(IS 2888:1983) according to which "toilet soaps" are grouped into three grades i.e., Grade 1, 2 and 3 with the 'total fatty matter' (TFM) requirement for each grade at minimum of 76, 70 and 60 per cent, respectively. It was also stated that "bathing bar" was not covered under the provisions of the Drugs and Cosmetic Act/Rules, at present. Accordingly, a 'toilet soap' must have a TFM content of 60 per cent, at the least. Bathing bars having a TFM content of less than 60 per cent cannot be regarded as 'toilet soap' and should not be marketed and cleared as a toilet soap.

Sub-heading 3401.10 of the Tariff, covers "soap in any form". As per explanatory notes below the aforesaid sub-heading of H.S.N., soaps of this heading are categorised as (i) hard soaps (which are usually made with sodium hydroxide or sodium carbonate);(ii) soft soaps (which are made with potassium hydroxide or potassium carbonate) and they may contain small quantities not exceeding 5 per cent of synthetic organic surface active agents (OSAA); and (iii) liquid soaps. This heading covers in particular the (i) toilet

soaps, (ii) house hold soaps, (iii) rosin, tall oil or napthenate soaps; and (iv) industrial soaps.

Audit scrutiny revealed that the instructions dated 15 April 1993 issued by the Director General Health Services were not given effect, while classifying 'soaps' in the Tariff. There is no mention about TFM requirement for classification of soap in the said schedule. Bathing bars containing less than 60 per cent TFM content would neither be "toilet soap" although being classified under sub heading 3401.10 nor as other soaps (washing soap) because of the OSAA contents remaining less that 5 per cent. In commercial parlance also bathing bars are different from toilet soaps.

In five Commissionerates, test check of records revealed that nine assessees had cleared bathing bars by classifying them as 'soaps' under heading 34.01 and paid duty of Rs.240.87 crore from 1994-95 to 1996-97, notwithstanding the fact that the TFM contents of each one of them was far less than the minimum required percentage of 60 per cent and were therefore not 'soaps' in terms of the Drug Controller's instructions cited above. There is therefore, a need for a distinct classification of these items.

3.7 Evasion of duty by suppressing production

According to rule 53 of the Rules, every manufacturer is required to maintain a daily stock account of finished products in the prescribed form (RG-I).

In seven Commissionerates, test check of records revealed ten cases of suppression of production and consequential non-levy of duty of Rs.3.66 crore.

One such case is illustrated below:

A comparison of the production figures as depicted in the balance sheet and that entered in RG-I register of an assessee, in Chandigarh Commissionerate, for the period January 1994 to December 1994, revealed a production difference (shortfall) of 5619.072 tonne (as per balance sheet-35977 tonne and as per RG-I register 30357.928 tonne) of

'detergent powder'. The suppression of production had resulted in duty of Rs.3.18 crore not being levied.

On being pointed out (March 1997), the department attributed the difference to a clerical mistake in reflecting the figures of production in the balance sheet. The reply of the department is not tenable because the revised figures submitted later were also not reconcilable with those entered in the relevant excise records.

3.8 Exemptions

As per section 5A (1) of the Act, Government is empowered to exempt excisable goods from the whole or any part of the duty leviable thereon conditionally or unconditionally.

In four Commissionerates, test check of records revealed inadmissible grant of exemptions involving duty effect of Rs.2.76 crore in four cases.

Two of these cases are illustrated below:

i) According to notification No.88/88-CE dated 1 March 1988, as amended, detergents manufactured by KVIC are exempt from whole of the duty of excise leviable thereon. Audit scrutiny, however revealed that certain big manufacturers/brand name owners who were not eligible for such exemption availed the above exemption from duty by getting their branded goods manufactured through KVIC.

An assessee, in Delhi Commissionerate, manufacturing a branded detergent powder also got the branded goods manufactured through two KVIC units. During the period 1993-94 to 1995-96, the assessee purchased 9914.15 tonne of branded detergent powder valuing Rs.8.19 crore from these KVIC units and was able to avoid payment of duty of Rs.2.45 crore. The lacunae in the notification needs to be plugged by a suitable amendment to the aforesaid notification, on the lines of notification No.1/93-CE dated 28 February 1993 (now 16/97-CE dated 28 February 1997) where SSI exemption is denied to the assessees manufacturing branded goods for others.

ii) According to the notification dated 1 March 1988, as amended, synthetic detergents are exempted for whole of the duty of excise leviable thereon provided such detergents are manufactured in rural areas by women's society or institutions recognised by KVIC. Further, according to explanation (a) under the said notification, "rural area" means area comprised in any village and includes area comprised in any town, the population of which does not exceed ten thousand.

An assessee, in Calcutta Commissionerate, engaged in the manufacture of synthetic detergents (sub-heading 3402.90) cleared goods valuing Rs.1.54 crore between April 1994 and May 1996 without payment of duty in terms of the notification dated 1 March 1988, notwithstanding the fact that his unit was located in Calcutta Metropolitan Planning Area since July 1991 and was not covered under the definition of "rural area". Since the basic condition for availing the exemption was not fulfilled, availment of exemption involving duty effect of Rs.24.87 lakh during 1994-95 and 1995-96 was not correct.

3.9 Financial accomodation to the assessees

Under section 11 A of the Act, for non-payment of duty on account of any reason, duty can be recovered from the manufacturer by issue of a 'show cause notice' normally within a period of six months only, excepting cases of fraud, willful misrepresention with the intent to evade duty, in which case the above period is extendible to 5 years. Prior to 26 May 1995, there was no provision in the Act or the Rules to charge interest for such non-payment or short payment. However, from 26 May 1995, interest on delayed payment is normally chargeable only after 3 months from the date of confirmation of the demand and not from the relevant date of clearances (section 11 AA). (Only in cases of fraud etc., interest is leviable from the relevant dates of clearances (section 11 AB).

Considering the fact that in the event of non-payment of duty or part payment of duty, the Government dues are available to the assessee for his own purposes which would not have been free of charge, had the assessee borrowed the same amount, the Supreme Court in the case of Oswal Agro {ECR 5 (SC) 1996} laid down that in such

cases interest at bank rates should be charged from the assessee in respect of the entire period during which the Government dues remained with the assessee. In the absence of provision for charging any interest prior to 23 July 1996 and even thereafter for charging interest not from the relevant date of clearances, delays in adjudication lead not only to non-recovery of Government's dues but also to financial accomodation to the assessee at the cost of exchequer, by way of loss of interest.

Test check of records revealed loss of revenue of Rs.21.09 crore on account of interest lost and time-barred demands, as tabulated below:-

Reasons	**No. of assessees**	**Amount of duty not paid**	**Loss of revenue**
		(Amount in crore of rupees)	
Delay in adjudication	9	18.16	5.98 (interest)
Non-recovery of confirmed demand	1	2.15	1.93 (interest)
Duty paid in instalments without interest	4	3.59	0.33 (interest)
Delay in finalisation of provisional assessments	7	9.04	4.02 (interest)
Non-vacation of stay orders	1	8.58	7.53 (interest)
Demand had become time barred due to departmental inaction	3	1.48	1.30 (demand)
Total	**25**	**43.00**	**19.79 (interest)** **1.30 (demand)**

In one case of delay in adjudication, the department accepted the facts (July 1997).

3.10 Other cases

i) Modvat credits

In 23 Commissionerates, inadmissible (for various reasons like items not covered under Modvat scheme, non-filing of required substantive returns for claiming Modvat, etc.) availment of Modvat credits of duty paid on inputs and capital goods involving Rs.7.58 crore by 39 assessees were noticed. Of these, department accepted objection involving credit of Rs.12.24 lakh in 6 cases and reported recovery of Rs.7.66 lakh, besides issue of SCN for Rs. 1.50 crore.

ii) Unverified Modvat invoices

To check the misuse (fraudulent use) of invoices issued by a supplier which become the basis of Modvat credit being claimed by the buyer manufacturer, the Board through it's circular dated 28 May 1986, instructed that these invoices should be sent back to the originating range offices for cross-verification to check whether these invoices were genuine. Test check of records in 15 Commissionerates revealed that about 35 per cent (71318 out of 205744 invoices relating to the year 1994-95 to 1996-97) of these Modvat invoices were not sent for cross-verification to the originating range offices. Further, even for the invoices (134426 invoices) which were sent for cross verification, the verification reports on 98174 (73 per cent) were not received back. In the absence of the invoices being sent for cross-verification and non-receipt of the reports thereon, the correctness of credits taken on these could not be verified in audit.

iii) Money credit

In five Commissionerates, test check of records revealed incorrect availment/utilisation of money credit of Rs.26.57 lakh in five cases on account of various reasons like availing of the credit of lapsed accumulated balance, availing of credit on minor oils not used in the manufacture of the specified final products (soaps) etc.

iv) Exemptions to SSI units

In six Commissionerates, eight cases of grant of inadmissible/unintended exemptions, involving short levy/non-levy of excise duty amounting to Rs.47.46 lakh were noticed.

v) Physical verification of stock

In 21 Commissionerates, test check of records of 84 assessees manufacturing soaps and other surface active agents revealed that the physical verification of stock had not been conducted at all for long periods, though required to be done so by the department as often as deemed necessary (under rule 223 A), as shown below:

Period for which verification of stock pending	No. of assessees
For the last 2 years	10
For over 2 to 5 years	49
For over 5 to 10 years	25

vi) Norms of production not fixed

In 24 Commissionerates, test check of records of 114 assessees revealed that norms of production were not fixed by the department, as required under rule 173 E. In the absence of the fixed/prescribed norms, the correctness of production of finished goods as accounted for by the assessees could not be verified.

vii) Periodical returns

In 25 Commissionerates, test check of records revealed that 104 assessees did not submit the prescribed returns (RT 5 under rule 55) depicting, inter-alia, quantities of raw material used, quantities of finished goods manufactured, during the last three years and the department also did not insist that the prescribed returns be filed by the manufacturers.

The reply of the Ministry on the above points has not been received (November 1997).

4.1 Central excise duty collected but not paid to Government

As per section 11D (1) of the Act, every person who has collected any amount from the buyer of any goods in any manner as representing duty of excise, shall forthwith pay the amount so collected, to the credit of the Government.

Four units of public sector corporations, in Rajkot Commissionerate, imported motor spirit, high speed diesel, superior kerosene oil, furnace oil and aviation turbine fuel on which customs and countervailing duty had been paid. These items alongwith their indigenous products were sold after charging the central excise duty at appropriate rate.

The central excise duty so collected from the customers on imported products was not remitted to Government on the plea that the imported products had already suffered customs and countervailing duty and that no central excise duty was attracted since no further manufacture was involved. Between March 1996 and February 1997, the assessees collected central excise duty of Rs.661.22 crore as excise duty from their customers on the sale of imported petroleum products, without remitting it to Government according to section 11 D(1) of the Act.

Reply of the Ministry has not been received (November 1997).

4.2 Delay in implementation of ad valorem rates of duty

In accordance with the provisions of section 62 (b) and Fourth Schedule of the Finance Act, 1994, the duty structure on "tyres and tubes" was to be changed from specific plus ad valorem rates to ad valorem rates. It was provided in the Act, ibid, that this amendment would come into force from a date to be notified by the Central Government. Although the Finance Act was enacted from 13 May 1994, the relevant notification bringing into force the said amendment, was issued only from 1 March 1997.

a) Test check of four tyre manufacturers in Aurangabad (2), Chennai (1) and Mumbai (1) Commissionerates, disclosed a revenue loss of Rs.71.78 crore from May 1994 to February 1997 due to delay in implementing the ad valorem rates of duty for this sector. The actual collections for this period were based on the specific rates of duty which amounted to Rs.4019.27 crore. The difference in duty paid at specific rates and that payable on ad valorem rates worked out to 45.59 per cent in test check cases, based on which the overall revenue loss to the Government attributed to delay in implementing an expressed policy and intent of the Parliament would work out to Rs.1756.03 crore.

b) While the ad valorem rates were not given effect to by the Ministry, it was observed that the Ministry did not even revise the specific rates in consonance with the rising prices of tyres, during the period. In case of an assessee (Chennai Commissionerate) alone, it was observed that while the selling prices of different types of tyres had been increased on four occasions (1 September 1994, 1 January, 1 April and 1 June 1995), the specific rates were revised only once on 16 March 1995. In the absence of ad valorem rates, the non-revision of specific rates periodically, led to a short collection of duty of Rs.11.68 crore from September 1994 to February 1997.

Reply of the Ministry has not been received (November 1997).

4.3 Delay in revision and non-fixation of tariff value

a) The Government, by notification dated 1 November 1995, had fixed the tariff values for aerated water for different sizes of the bottles based on maximum retail price (MRP) of each bottle.

The fixation of tariff value at lower rates and its non-revision subsequently on increase in MRP of three sizes of bottles (250/300 ml, 500 ml and 1000 ml) in January 1996 and October 1996, leading to short levy of duty of Rs.31.05 crore, was pointed out in November 1996 (Para 4.4 of Audit Report for the year ended 31 March 1996). Despite this, no action was taken by the Ministry to revise the tariff values. The tariff values of the three sizes of bottle were revised from 29 April 1997. The delay in revision of tariff value allowed the manufacturers to pay duty on the lower tariff value fixed in November

1995, thereby resulting in further short realisation of revenue of Rs.30.91 crore from 1 November 1996 to 28 April 1997.

b) It was further noticed that even while revising the tariff value of other sizes of the bottle on 29 April 1997, the tariff value of 1500 ml. bottle was not fixed. The pattern of the marketing of this size of bottle was the same as for other sizes of the bottles. There was, therefore, no reason to exclude the bottle of the size of 1500 ml. from fixation of tariff value, by the Ministry.

Three units in three Commissionerates, engaged in the manufacture of aerated waters, declared MRP of Rs.38 per bottle of 1500 ml. They cleared their products paying duty on the assessable value which was much lower than what it should have been, had the assessable value been fixed on the basis of the parameters applied by the Ministry for fixing the tariff values. The non-fixation of tariff value for bottle of 1500 ml. resulted in short realisation of duty of Rs.2.78 crore (approximately) during February 1996 to June 1997 from these units alone.

Reply of the Ministry has not been received (November 1997).

4.4 Inconsistent approach of the Ministry/department to the benefit of assessee

An assessee, in Vadodara Commissionerate, manufacturing goods falling under chapters 26, 28 and 38 of the Tariff, had classified one of its products "safolite solution (sodium formaldehyde sulphoxylate solution)" under sub-heading 2831.90 and cleared the entire production to its sister unit at a price fixed on cost data basis, for converting the solution into chips/powder. Since the price fixed on cost data basis did not include manufacturing overheads and profits, there was undervaluation to that extent and consequent short levy of duty of Rs.1.32 crore was pointed out to the Ministry in August 1995.

The Ministry contended (December 1995) that the product was neither marketable ordinarily nor sold in commercial market, therefore overheads or profitability of non-marketable commodity were not comparable to normal profits or overheads.

Since safolite solution not being marketable was not an excisable commodity in terms of facts disclosed by the Ministry and in view of Supreme Court judgement in the case of M/s. Bhor Industries Limited {1989 (40) ELT 280}, the matter was re-examined in audit on the question of availment of Modvat credit by the assessee on such non-excisable goods. The records revealed that Modvat credit of Rs.8.82 crore was availed on inputs used in the manufacture of safolite solution during April 1993 to June 1996 by the assessee and Modvat credit of Rs.9.82 crore of the duty paid on safolite solution, was availed by its sister unit during the same period. Since Modvat credit is admissible only on specified excisable commodities, availment of credit of Rs.18.64 crore was, therefore, incorrect.

On being pointed out in audit (October 1996), the department went back on its earlier stand and stated (December 1996) that product was marketable but the assessee had chosen not to market it. The department however, issued a show cause notice for Rs.10.69 crore for the period from April 1993 to September 1996, to protect Government revenue.

The reply of the department is not tenable and also not consistent, as it contradicts its earlier stand and is contrary to the Supreme Court Judgement cited above. Further, a product cannot become marketable for the purpose of availing Modvat credit when it is treated as non-marketable for the purpose of valuation.

4.5 Unintended benefit on petroleum products

In the Budget 1996-97, excise duty on specified petroleum products like furnace oil, low sulphur heavy stock, light diesel oil, raw naphtha etc. was increased from 10 to 15 per cent, ad valorem. To ensure that the prices of these products were not affected consequent upon the increase in duty, the incidence of the increase in duty was to be passed on by the oil companies to the Oil Pool Account, being maintained by the Ministry of Petroleum and Natural Gas and not to the consumers. However, no mechanism appeared to have been evolved by the Ministry to ensure that this was implemented.

Test check of records of sixteen units of four public sector oil companies, in seven Commissionerates, disclosed that while oil companies had actually charged duty at 10 per cent ad valorem from the buyers, the amount of excise duty on the face of the Modvat invoices were shown at 15 per cent ad valorem. Because of the wrong depiction, the buyer manufacturers became entitled to avail the Modvat credit of duty at 15 per cent ad valorem instead of at 10 per cent which was the correct rate at which duty was actually paid. Accordingly, the buyer manufacturers would have availed an excess credit (i.e. difference of 5 per cent) of Rs.9.07 crore between August 1996 and June 1997.

Reply of the Ministry has not been received (November 1997).

5. DEMANDS DELAYED OR NOT RAISED

Some of the illustrative cases of demand not being raised or raised with delay are given in the following paragraphs:

5.1 Demands not raised

Under rule 13 and notifications issued thereunder, goods can be cleared for export without payment of duty but under bond. The rules and notifications further require that the goods in question should be exported within six months from the date of clearance from the factory or warehouse and proof of export furnished. Rule 14 A provides for issue of a demand by the proper officer for duty leviable on the goods, if proof of export is not produced by the manufacturer within the prescribed period of six months. However, Commissioner may extend period of six months in a particular case.

i) A public sector undertaking, in Visakhapatnam Commissionerate, cleared goods involving a duty of Rs.131.51 crore for export between April 1994 and January 1996 under bond. Neither the assessee produced proof of export within the stipulated period (even upto August 1996) nor did the department take any action for raising the demand and recovering the duty.

On being pointed out (August 1996), the department confirmed the facts and stated (March 1997) that necessary action had since been taken for admittance of proof of export, leaving goods involving duty of Rs.38.53 crore for which proof of export was not produced by the assessee. Action taken to recover duty of Rs.38.53 crore has not however, been intimated (November 1997).

Reply of the Ministry has not been received (November 1997).

ii) Twelve assessees, (Bangalore (1), Belgaum (1), Chandigarh (1), Cochin (1), Hyderabad (1), Jamshedpur (2), Mumbai I (1), Mumbai III (3), and Nagpur (1), Commissionerates) cleared their products without payment of duty for the purpose of export between July 1991 and November 1995. The proof of exports were not produced

by the assessees even after the lapse of more than six months nor was the duty paid. Action was also not taken by the department to raise demand and recover duty of Rs.1.65 crore due thereon.

On being pointed out (between May 1994 and February 1997), the department admitted the objection in five cases involving duty of Rs.91.19 lakh. In four other cases, show cause notices were issued for Rs.40.58 lakh. Reply in the remaining three cases has not been received (November 1997).

The Ministry admitted (September and December 1997) the objection in three cases but contended (June 1997) in one case that the matter was in the knowledge of the department and assessee was being pursued for submission of proof of export. Reply in the remaining eight cases has not been received (November 1997).

Reply is not tenable as goods were cleared for export between March and November 1994 and no show cause notice was issued till date of audit viz., November 1995. Show cause notice was issued only in June 1996 and the duty due had not been recovered till August 1997.

5.2 Non-realisation of confirmed demands

For settlement of disputes between Government departments and public sector enterprises etc., a Committee of Secretaries was formed in December 1991 by the Government. Accordingly, three cases of confirmed demands of Rs.42.07 crore, not barred by stay orders and pending recovery by Vadodara Commissionerate, since October 1991, December 1991 and August 1993 from a public sector undertaking were referred to this Committee. Based on Committee's decision, the Board in December 1992, January and October 1993, directed the Commissionerate to effect the recovery immediately. Despite these directives, recoveries were not made resulting in blocking up of government revenue of Rs.42.07 crore and non-recovery of interest of Rs.29.57 crore from the date of demand to March 1997.

On being pointed out (October 1994), the department contended (January 1995) that the Committee had redecided in May 1994 that the public sector undertaking and the department should pursue the Tribunal jointly for early decision of their pending case.

The reply is not tenable as the fact remains that the department did not recover the dues even after getting favourable decision as early as in December 1992. Had the recoveries been effected in time, the question of reviewing their earlier decision by the Committee of Secretaries, would not have arisen.

5.3 Delay in adjudication of demands

The Public Accounts Committee in its 84th Report (1981-82) had adversely commented on the inordinate delays in finalisation of adjudication proceedings in demand cases. Accordingly, the Board had issued instructions dated 17 January 1983, requiring earnest efforts being put in by the adjudicating officers to adjudicate the demand cases expeditiously. It was also stressed that the demand cases should be adjudicated within a maximum period of six months from the date of issue of show cause notice.

i) An assessee, in Mumbai III Commissionerate, was served show cause cum demand notice for Rs.16.40 crore on 4 December 1992 for irregular removal of non-texturised polyester yarn. The demand was confirmed on 30 August 1996. On an appeal filed before Tribunal against the said order, the Tribunal directed the assessee to deposit the said amount which was paid by the assessee on 29 March 1997.

The facts of the case revealed that the case was not pursued properly after issuing show cause notice and delay for 3 years and 8 months in deciding the case, resulted in financial accomodation to the assessee, by way of interest of Rs.10.63 crore. Further, interest of Rs.1.07 crore leviable on the confirmed amount under section 11AA from December 1996 was also not levied.

This was pointed out in April 1997; reply of the Ministry/department has not been received (November 1997).

ii) In Mumbai III Commissionerate, show cause notices to two units of an assessee were served between April 1995 and January 1996 demanding duty of Rs.1.69 crore on account of incorrect classification of multilayer laminated plastic tubes. The demands were not adjudicated inspite of fact that a similar issue relating to third unit of the same assessee was decided on 27 December 1995 and the classification list of the product of second unit of the same assessee was approved on 28 May 1996. Though there was no reason to keep these demands pending, yet these were not finalised/adjudicated. This resulted in blocking up of Government revenue of Rs.1.69 crore and financial accomodation to the assessee, by way of interest of Rs.18.38 lakh.

This was pointed out in November 1996 and February 1997. Reply of the Ministry/department has not been received (November 1997).

iii) In Mumbai I Commissionerate, show cause notices for Rs.2.99 crore were issued between October 1994 and December 1996 to an assessee, disallowing him deduction claimed towards crate hire charges from the assessable value. The demands were not adjudicated till March 1997, inspite of the fact that the Tribunal had also decided in the case of M/s. Vijayawada Bottling Company Limited {1993 (68) ELT 104} that such charges were not allowable deductions from the assessable value. This resulted in blocking up of Government revenue of Rs.2.99 crore and financial assistance to the assessee of Rs.70.61 lakh, by way of interest upto March 1997.

This was pointed out in February and May 1997. Reply of the Ministry/department has not been received (November 1997).

iv) Calcutta II Commissionerate issued show cause notices demanding duty of Rs.83.92 lakh between April 1990 to May 1994, to a tyre manufacturer on the basis of an audit objection on incorrect classification of tyres and tubes. Though the incorrect classification was admitted by the Ministry in November 1988 and again in November 1990, the show cause notices were not adjudicated. The inordinate delay in adjudication resulted in blocking up of Government revenue of Rs.83.92 lakh and financial assistance to the assessee company by way of interest of Rs.49.21 lakh.

On being pointed out (March 1995 and March 1997), the department admitted the delay and stated (October 1995) that efforts were being made to adjudicate the cases.

Reply of the Ministry has not been received (November 1997).

v) A public sector undertaking, in Meerut Commissionerate, was served with two show cause cum demand notices in November 1987 demanding duty of Rs.7.72 crore, short paid on electrical machines cleared from March 1975 to November 1980. Although more than nine years have elapsed, the case has not been adjudicated. This resulted in blocking up of Government revenue amounting to Rs.7.72 crore and financial assistance to the assessee, by way of interest of Rs.12.50 crore.

On being pointed out (October 1995 and December 1996) the department stated (November 1996) that the issue of inclusion of the value of bought out items in the assessable value of the goods was decided many times against the department by various Courts/Tribunals.

The reply of the department is not relevant as show cause cum demand notices issued nine years back have still not been adjudicated.

vi) An assessee, in Jamshedpur Commissionerate, was issued five show cause cum demand notices for Rs.5.12 crore between 1991 and 1995 on account of incorrect classification of parts of conveyor systems. Audit scrutiny revealed that the case was not properly pursued and demands were not adjudicated resulting in blocking up of Government revenue of Rs.5.12 crore and financial assistance to the assessee amounting to Rs.3.71 crore, by way of interest.

On being pointed out (January 1997), the department stated (February 1997) that the adjudication could not be done as the correct classification had not yet been decided. The fact, however, remains that the case had not been adjudicated, as a result Government money remains unrecovered, to the benefit of the assessee.

Reply of the Ministry has not been received (November 1997).

5.4 Delay in raising demand

A public sector undertaking, in Shillong Commissionerate, was issued show cause notice demanding duty of Rs.59.75 lakh on 25 November 1994. While adjudicating the case on 9 March 1996, the adjudication officer held the demand as time barred. The failure of the department to issue the show cause notice in time resulted in loss of revenue of Rs.59.75 lakh.

On being pointed out (September 1996), the department stated (May 1997) that it would be premature to say that the delay had resulted in the loss of revenue as the Committee of dispute in its meeting on 21 September 1995 had directed the assessee to resolve the matter through mutual discussion.

The reply of the department is neither relevant nor tenable as the department itself had declared the demand as time barred in its adjudication order dated 9 March 1996, which was passed after the meeting of 21 September 1995.

Reply of the Ministry has not been received (November 1997).

6. NON-LEVY OF DUTY AND INTEREST

Under rule 53 of the Rules, every manufacturer is required to maintain daily stock account in a prescribed form indicating inter-alia, the description of goods, quantity manufactured and quantity removed for various purposes. Rules 9 and 49 prescribe that excisable goods shall not be removed from the place of manufacture or storage unless the duty leviable thereon, has been paid. If any manufacturer, producer or licencee of a warehouse, removes excisable goods in contravention of these rules or does not account for them, besides such goods becoming liable to confiscation, a penalty not exceeding three times the value of goods or five thousand rupees, whichever is greater, is also leviable under rule 173Q.

Some illustrative cases of non/short accountal of goods or removal of goods without payment of duty are given in the following paragraphs:

6.1 Duty not levied on production not recorded

An assessee, in Mumbai III Commissionerate, manufactured coconut oil in HDPE bottles and cleared it without payment of duty treating it as non-excisable. Scrutiny of records revealed that the classification list of the same product was approved by the department on 15 March 1993 for purposes of export, classifying it under sub-heading 3305.90. Samples were also taken on 7 January 1994 for chemical test which disclosed that the product was a preparation containing vegetable and paraffin oils conforming to 'hair oils' under chapter 33. However, no action was taken by the department to ensure that the assessee maintained the requisite excise records and paid duty accordingly. Non-levy of duty of Rs.42.24 crore during April 1992 to December 1994 was estimated in audit on the basis of average production and the department was asked to work out the actual non-levy.

On being pointed out in audit (January 1995), the department stated (April 1997) that the issue was already taken up by them and the sample was drawn on 16 January 1995.

The reply is not tenable as no action was taken to quantify the duty liability and raise demand till the date of audit (viz 6 January 1995). Further, even till July 1997, duty for the period prior to January 1995 had not been determined and demanded.

Subsequent verification revealed issue of the show cause notices for Rs.21.18 crore for the period January 1995 to October 1996.

Reply of the Ministry has not been received (November 1997).

6.2 Duty not levied on goods not re-warehoused

Under rule156A read with rules 156B and 173N of the Rules, excisable goods can be cleared under bond from a factory or warehouse to another, subject to production of re-warehousing certificate within ninety days of removal of goods or such extended period as the Commissioner may allow. If re-warehousing certificate is not produced within the stipulated period, the duty is to be demanded by the Range Superintendent of the consignor's factory.

i) A public sector corporation, in Mumbai II Commissionerate, cleared "high speed diesel oil" to its various depots under bond, for re-warehousing between May 1993 and November 1994. However, some consignments were not re-warehoused whereas others were warehoused short at the warehouses of destination, as revealed by the absence of re-warehousing certificates or the information therein. No action was taken by the department for recovery of duty of Rs.11.62 crore.

On being pointed out (July 1995), the department stated (March 1996) that show cause cum demand notices had been issued for an amount of Rs.10.80 crore.

Reply of the Ministry has not been received (November 1997).

ii) Two assessees, in Hyderabad and Visakhapatnam Commissionerates, cleared 56 consignment of goods between June 1994 and May 1995 for re-warehousing. However, the re-warehousing certificates were neither produced by the assessees to the proper officer nor was any action taken by the department to recover duty, even after the lapse of

ninety days from the date of clearance of goods. The duty recoverable on the goods so cleared was Rs.78.51 lakh.

On being pointed out (October 1995 and March 1996), Visakhapatnam Commissionerate intimated (December 1996) issue of show cause notices for Rs.64.02 lakh.

The Ministry admitted objection relating to Hyderabad Commissionerate (October 1997). Reply relating to Visakhapatnam Commissionerate has not been received (November 1997).

6.3 Non-levy of additional duty

i) As per section 3 of the Additional Duties of Excise (Textiles and Textile Articles) Act, 1978, additional excise duty is leviable at 15 per cent of the amount of basic excise duty chargeable. For the purpose of determining additional excise duty, the basic excise duty is required to be calculated after excluding any exemption for giving credit or for reduction of duty already paid on raw material used in the production or manufacture of such goods.

Four assessees in Ahmedabad, Aurangabad, Rajkot and Vadodara Commissionerates, manufactured woollen tops, woollen yarn and synthetic staple fibre etc. and captively consumed the same without payment of basic excise duty, availing exemption under notification dated 11 August 1994 and 16 March 1995, as amended. However, no additional duty though leviable under the Act, ibid, was levied, by working out correctly the quantum of basic excise duty chargeable after excluding the benefit availed through the above exemption notification. This resulted in non-levy of additional duty of Rs.52.08 lakh from September 1994 to October 1995.

On being pointed out (between February 1996 and March 1997), the department accepted the objection in one case and issued show cause notice for Rs.17.22 lakh. In the remaining cases, the department contended (between June and September 1996) that the exemption granted under notifications dated 11 August 1994 and 16 March 1995 cannot

be equated with the exemption notifications mentioned in excluded category of section 3 of the Act, ibid.

Reply is not acceptable since the aforesaid notifications fall under excluded category as they exempt duty payable on inputs which are consumed captively in manufacture of dutiable final products.

Reply of the Ministry has not been received (November 1997).

ii) An assessee, manufactured, inter alia, coated fabrics (heading 59.03) out of base fabrics procured from its sister concern without payment of duty under rule 96 D allowing removal of cotton fabrics without payment of duty from one factory to another processing factory. The base fabrics after curing process were consumed captively, without payment of additional duty leviable under the Additional Duties of Excise (Goods of Special Importance) Act, 1957, between October 1994 and July 1995.

On being pointed out (September and November 1995), the department replied (January/July 1996) that a study of the manufacturing process revealed that from the base fabrics a new product namely "stiffened fabric" appropriately classifiable under sub-heading 5901.90 emerged and therefore, duty amounting to Rs.47.17 lakh due for the period from 1 May to 13 November 1995 had been confirmed. Action taken for recovery of duty for the earlier period was not intimated (November 1997).

Reply of the Ministry has not been received (November 1997).

6.4 Evasion of duty by suppressing production

i) A comparison of RT-12 (monthly abstract of RG 1) with the annual accounts for the period from March 1993 to June 1995 of an assessee, in Visakhapatnam Commissionerate, revealed that production of 13564 four wheeler tyres was short accounted for in central excise records. This resulted in duty evasion of Rs.36.62 lakh.

On being pointed out (August 1996), the department admitted the objection and stated (April 1997) that action was being taken to issue show cause notice.

Reply of the Ministry has not been received (November 1997).

ii) A comparison of the annual physical verification report of stock with daily stock account (RG-1) in a public sector steel plant, in Bhubaneswar Commissionerate, revealed that production of 2817 tonne of iron and steel slabs was short accounted for in the RG-1 account, during the period 1995-96. This resulted in escapement of duty of Rs.28.73 lakh.

This was pointed out in November 1996. Reply of the Ministry/department has not been received (November 1997).

iii) Scrutiny of the annual accounts published by an assessee, in Bolpur Commissionerate, disclosed that 385 tonne of core lamination was sold during the year 1993-94, while duty was paid on 262 tonne only, as recorded in the central excise records. The production and clearance of 123 tonne was thus, short accounted for in the central excise records, resulting in evasion of duty amounting to Rs.24.91 lakh.

On being pointed out (December 1994), the department contended (November 1996) that the sale figure shown in the annual accounts was inclusive of goods cleared without payment of duty on completion of job work on the raw materials received by the assessee from customers under rule 57F(2).

The contention of the department is not tenable as the materials received under rule 57F (2) for job work belonged to the customer and therefore the question of sale of such processed goods to the customer did not arise.

Reply of the Ministry has not been received (November 1997).

iv) An assessee, in Jamshedpur Commissionerate, reduced 3464 tonne of pooled iron from closing balance in the month of June 1995, being an adjustment of difference between the estimated and actual weight of pooled iron. Such a reduction of quantity from RG 1 was incorrect as there was no provisions in the Rules for granting permission

for such reduction in the production account. This resulted in escapement of duty of Rs.15.15 lakh.

On being pointed out (July 1996), the Ministry admitted the objection and intimated (June 1997) issue of show cause notice for Rs.15.15 lakh with imposition of penalty.

6.5 Duty not levied on goods consumed captively

As per note 2 under chapter 52 and 55, bleaching, mercerising, dyeing, printing, water-proofing, shrink-proofing, organdie processing or any other process or any one or more of these processes, shall amount to 'manufacture'.

A cotton mill, in Calcutta II Commissionerate, obtained grey fabrics of chapter 52 and 55 from outside on payment of duty and carried out the processes of bleaching, mercerising and dyeing. Since such processes amounted to manufacture as per note 2 of chapter 52 and 55, no exemption was available on the intermediate products emerging out of these processes. Duty was, therefore chargeable at each such stage and Modvat credit taken, if admissible otherwise. However, the assessee did not pay duty on intermediate products and this resulted in non-levy of duty of Rs.25.91 lakh on the intermediate products captively consumed during 20 May 1994 to 10 August 1994.

On being pointed out (December 1995), the department contended (January 1996) that though bleaching, mercerising and dyeing were very much manufacturing processes, they were, however, to be considered as a single process upto the stage of finished product when duty was finally paid by the assessee. Reply is not tenable in view of note 2 of chapter 52 and 55. However, a show cause cum demand notice was issued by the department in June 1996.

Reply of the Ministry has not been received (November 1997).

6.6 Non-levy of interest

i) Interest under Excise Act

As per section 11AA of the Act, where a person chargeable with duty determined under sub-section (2) of section 11A, fails to pay such duty within three months from the date of such determination, he shall pay, in addition to the duty, interest at 20 per cent per annum on such duty from the date immediately after the expiry of the said period of three months till the date of payment of such duty.

a) Mumbai III Commissionerate, after approving on 27 April 1995, the price lists of coco powder, drinking chocolate and coco butter, directed the assessee to pay the differential duty immediately. In compliance with these orders, the assessee paid the differential duty of Rs.1.57 crore between August 1995 and August 1996. Since duty was paid after three months from the date of determination of duty, interest of Rs.23.91 lakh for the period 26 August 1995 to 5 August 1996 was leviable, which was not levied. In addition, the assessee obtained an additional financial accommodation of Rs.3.26 lakh for non-payment of interest till April 1997.

This was pointed out in November 1996. The reply of the Ministry/department has not been received (November 1997).

b) In Belgaum Commissionerate, a stay order of High Court, relating to a confirmed demand of Rs.19.01 lakh for the period July 1991 to March 1992 against a manufacturer of veneer timber boards, was got vacated in September 1995. The assessee paid duty in instalments till November 1995, leaving a balance of Rs.4.98 lakh. Demand for the subsequent period April 1992 to May 1995 for Rs.78.39 lakh was also confirmed in September and November 1995 and the assessee was permitted to pay the duty in 12 equal instalments from November 1996. Yet neither the duty nor the interest was paid by the assessee. The interest payable at 20 per cent per annum amounted to Rs.20.50 lakh.

On being pointed out (September 1996), the department replied (March 1997) that the assessee was being reminded to pay the dues along with interest and action was being taken to attach the plant and machinery.

Reply of the Ministry has not been received (November 1997).

c) In the case of an assessee, Hyderabad Commissionerate did not take any action for about nine years for recovery of cess of Rs.5.10 lakh, which was due from April 1985 to March 1987. The assessee paid dues on his own, in three instalments between November 1995 and February 1996. Inaction of the department, resulted in loss of interest of Rs.18.38 lakh.

On being pointed out (March 1988 and September 1996), the Ministry contended (October 1997) that there was no provision for levy of interest on delayed payments prior to 26 May 1995.

Reply is not tenable as interest was leviable as per Board's circular of October 1985. Further, the provisions of section 11 of the Act for immediate recovery by attaching excisable goods was also not invoked.

d) Jamshedpur Commissionerate confirmed three demands of Rs.2.51 crore between February and May 1996 against an assessee. The assessee paid the amount of Rs.1.46 crore in June 1996 and remaining amount of Rs.1.05 crore was paid on 2 November 1996. However, interest amounting to Rs.5.96 lakh, due on belated payment beyond three months from the date of determination, was not recovered.

On this being pointed out (November 1996), the Ministry stated (June 1997) that the assessee had since been asked to pay interest (April 1997). Further, report on recovery has not been received (November 1997).

ii) Interest under the Finance Act : Delayed deposit of service tax

Under section 68 of the Finance Act, 1994, the service tax collected during any calender month shall be paid to the credit of the Central Government by the 15th of the subsequent month. Section 75 of the said Act, further provides that in the event the person responsible for collecting service tax, fails to credit the tax or any part thereof to the account of the Government within the period specified, such person shall be liable to pay simple interest at the rate of one and one half per cent for every month or part of a month.

An assessee, in Chandigarh Commissionerate, had collected service tax of Rs.7.65 crore on taxable services rendered during the period July 1994 to June 1996. However, the service tax so collected in each month was deposited after delay ranging from one to three months. No action was taken to levy interest on delayed deposit resulting in non-levy of interest of Rs.17.45 lakh for late deposit of service tax.

On being pointed out (February 1996 and March 1997), the department issued show cause notices for 16.89 lakh.

Reply of the Ministry has not been received (November 1997).

iii) Interest under value based advance licensing scheme

According to clause V of customs notification dated 19 May 1992, Modvat credit is not admissible on inputs/raw materials used in the manufacture of goods to be exported under value based advance licence. However, the Ministry subsequently, vide its circular dated 10 January 1997, allowed reversal of Modvat credit availed in contravention of the value based advance licensing scheme provided interest at 20 per cent per annum is paid on belated reversal.

Three assessees, in Vadodara Commissionerate and one assessee in Chandigarh Commissionerate, availing the facilities provided under value based advance licensing scheme also availed the benefit of Modvat credit of Rs.1.83 crore of duty paid on inputs,

used in the manufacture of goods exported. The credit so taken, was utilised towards payment of duty on goods cleared for home consumption. As utilisation of credit was in contravention of the scheme, the assessees reversed credit of Rs.1.83 crore in July and August 1995 in their credit account. However, interest of Rs.55.17 lakh on such belated reversal of credit was neither paid by the assessee nor demanded by the department.

On being pointed out (July and November 1996), the department stated (April 1997) that Rs.53.19 lakh had since been recovered from three assessees. Reply in the remaining one case has not been received (November 1997).

The Ministry confirmed the facts in one case. Reply in the remaining three cases has not been received (November 1997).

6.7 Other cases

In five other cases of non-levy of duty, the Ministry/department while accepting the objections involving duty of Rs.26.83 lakh, reported recovery of Rs.17.89 lakh till November 1997.

7. GRANT OF EXEMPTIONS

As per section 5A(1) of the Act, Government is empowered to exempt excisable goods from the whole or any part of the duty leviable thereon either absolutely or subject to such conditions as may be specified in the notification granting the exemption.

Some of the illustrative cases of incorrect grant of exemption noticed in audit are given in the following paragraphs:

7.1 Incorrect grant of exemption of additional duty of excise

i) Processed fabrics

As per notification dated 11 August 1994, "input fabrics" were exempt from whole of the duty of excise and additional duty of excise provided final products were not exempt from payment of whole of the duty or were leviable to 'nil' rate of duty.

Ten assessees (Ahmedabad (1), Rajkot (1) and Surat (8) Commissionerates) captively consumed "input fabrics" for further manufacture of processed fabrics without payment of additional excise duty leviable under the Additional Duties of Excise (Goods of Special Importance) Act, 1957. As the final products (viz., processed fabrics) in these cases were exempt from basic excise duty, the above notification granting the exemption was not applicable and therefore, they were liable to pay additional excise duty on "input fabrics". Incorrect availment of exemption resulted in non-levy of additional excise duty of Rs.20.86 crore between April 1994 and June 1996.

On being pointed out (March/December 1996), the department contended (between April 1996 and February 1997) in nine cases that the notification dated 11 August 1994 was issued exercising powers under both the Acts, therefore, the expression 'duty of excise' appearing in the notification would be duty leviable under both the Acts. In the tenth case, it stated that no additional excise duty was leviable as the final product was cleared on payment of both the duties.

Reply of the department is not relevant as final product viz processed fabrics being exempt from duty, the exemption notification was not applicable . Reply in the tenth case is not based on facts as the final product being exempt was cleared on payment at nil rate of duty.

Reply of the Ministry has not been received either in these cases or in similar cases reported in August 1996 (Para 6.3 of Audit Report 1995-96).

ii) Rubberised dipped nylon tyre cord fabrics

As per notification dated 16 March 1995, specified excisable goods, manufactured in a factory and used as inputs in a factory in or in relation to the manufacture of final products, were exempt from payment of whole of duty of excise leviable thereon.

The Supreme Court in the case of M/s. Modi Rubber Limited {1986 (25) ELT 849} held that an exemption notification issued under rule 8(1) of the Rules, (now section 5A of the Act,) does not mean an exemption from special excise duty and additional excise duty unless such exemption notification also refers to the statutory provisions relating to special excise duty and additional duty.

An assessee, in Bangalore Commissionerate, manufactured rubberised dipped nylon tyre cord fabric falling under sub-heading 5902.10 and consumed it captively in the manufacture of tyres, tubes etc. without payment of duty of excise and the additional duty of excise, claiming exemption under the notification, ibid. As additional duty of excise leviable under Additional Duties of Excise (Goods of Special Importance) Act, 1957, was not exempt, this resulted in short levy of additional duty of excise of Rs.4.22 crore during April 1995 to April 1996.

On being pointed out (February 1997), the department replied (February 1997) that the payment of additional duty of excise does not arise as the tyre cord fabric had already suffered additional duty of excise. However, show cause notice had been issued covering the period from May 1996 onwards.

The reply of the department is not acceptable as notification dated 16 March 1995 has no reference to the provision of the Additional Duties of Excise (Goods of Special Importance) Act, 1957, as such the additional duty was leviable in terms of the Supreme Court decision referred to above.

Reply of the Ministry has not been received (November 1997).

iii) Processed nylon tyre cord fabrics

Another assessee, in Mumbai I Commissionerate, got manufactured nylon tyre cord fabrics from a job worker and used it in the manufacture of tyres after claiming exemption under the notification, ibid. As there was no specific provision which exempted the nylon tyre cord fabrics from payment of additional duty of excise, the grant of exemption was incorrect and resulted in short levy of additional duty of excise on processed nylon tyre cord fabrics of Rs.11.40 lakh during April 1995 to October 1995.

This was pointed out in May 1996; reply of the Ministry/department has not been received (November 1997).

7.2 Incorrect application of exemption notification

i) Natural gasoline liquid

Under notification dated 1 March 1984, natural gasoline liquid (NGL) was chargeable to concessional rate of duty of Rs.5.50 per kilo litre at 15^{o} centigrade if intended for use in the manufacture of fertilisers and ammonia. It was further provided that where the intended use was in the manufacture of ammonia and such ammonia was used elsewhere in the manufacture of fertilisers, its movement, storage, use, etc. had to be accounted for in accordance with the procedure prescribed in the rules 192 to 196 BB.

An assessee, in Surat Commissionerate, obtained NGL at concessional rate of Rs.5.50 per kilolitre from Oil and Natural Gas Commission and used it in the power plant and also for manufacture of ammonia cleared for industrial use. As the NGL was not used for the manufacture of fertilisers, the duty concession availed by the assessee was

not in order and resulted in short realisation of duty of Rs.11.54 crore during September 1993 to June 1994.

On being pointed out (August 1994), the department contended (September 1995) that the use of NGL in the manufacture of ammonia was technically possible through the media of fuel for the generation of steam which in turn was used in the manufacture of power that goes into manufacture of fertiliser. As regards ammonia cleared for industrial use, the draft show cause notice was under scrutiny.

The contention of the department is not acceptable in view of the fact that a specific condition laid down in the notification was not fulfilled. Further enquiry in the case showed that the department had issued three show cause notices amounting to Rs.9.89 crore covering the period November 1995 to February 1997. For the period from 6 December 1994 to 14 November 1995, the NGL was obtained by the assessee at full rate of duty. The department further intimated (May 1997) that the assessee paid Rs.10.40 lakh in November 1995 on account of NGL used for production of ammonia sold for non-fertiliser use.

Reply of the Ministry has not been received (November 1997).

ii) Bulk drugs

Under notification dated 1 March 1994, bulk drugs of chapter 28 and 29 were allowed a concessional rate of duty of 10 per cent ad valorem. Under the said notification, bulk drugs were defined to have the same meaning as assigned to it in the Drugs (Price control) Order, 1987. The said order was repealed on 6 January 1995. Government again allowed the same concession to bulk drugs other than certain specific items by notification dated 9 February 1995 in which the definition of bulk drugs was related to the Drugs and Cosmetics Act, 1940. Therefore, during the intervening period from 7 January 1995 to 8 February 1995, there were no "bulk drugs" under the Central Excise Law due to non-existence of Drugs (Price Control) Order, 1987 and, therefore, goods classifiable under heading 29.42 were to be charged at tariff rate of 20 per cent ad valorem.

Ten assessees, (Guntur (1) and Hyderabad (9) Commissionerates) manufacturing goods falling under heading 29.42, cleared their goods as bulk drugs at concessional rate of 10 per cent ad valorem between 7 January 1995 and 8 February 1995. As there were no `bulk drugs' under Central Excise Law during the period, the concessional rate allowed was incorrect. This resulted in a short levy of duty of Rs.98.70 lakh.

On being pointed out (between October 1995 and January 1997), the department contended (December 1996 and March 1997) that the intention of the Government was to continue the concession of March 1994, beyond 6 January 1995 even after Drugs (Price Control) Order, 1987 was repealed.

The reply of the department is not tenable as the notification dated 9 February 1995 cannot extend the benefit, retrospectively.

Reply of the Ministry has not been received (November 1997).

iii) Waste and scrap

Under a notification dated 16 March 1995, 'waste' and `scrap' arising in the course of manufacture of exempted goods was exempted from the whole of the duty of excise leviable thereon. By virtue of another notification dated 18 May 1995, this exemption was not made available to such waste and scrap, if dutiable goods were also manufactured in the same factory. Prior to 16 March 1995, no such exemption was available.

a) A public sector undertaking obtained 'waste' and 'scrap' of iron, steel and copper during the manufacture of excisable goods and cleared them from February 1994 to 15 March 1995 and June 1995 to July 1996 after availing exemption under the said notification. Availment of exemption was incorrect because prior to 16 March 1995, no such exemption existed and from 18 May 1995 assessee was not entitled to exemption because excisable goods were produced in the factory. This resulted in short levy of duty of Rs.82.02 lakh. It was also noticed that instead of issuing show cause notice, department issued a formal letter in May 1996 asking him to pay duty of Rs.24.51 lakh on

copper scrap and no action was taken for disallowing exemption on iron and steel scrap. The assessee had not paid the said amount till the date of audit (19 August 1996) and no show cause notice was issued to him. As regards iron and steel scrap, no action was taken by the department.

On being pointed out (between August 1996 and February 1997), the department stated (April and June 1997) that the assessee had paid Rs.20.63 lakh in August 1996 and added that an in-depth study was required to take appropriate action for recovery of remaining duty, if any. Further progresss has not been received (November 1997).

Reply of the Ministry has not been received (November 1997).

b) Another assessee, in Bolpur Commissionerate, cleared waste and scrap of steel falling under chapter 72, arising during the course of manufacture of different goods and availed exemption under notification dated 18 May 1995, on the ground that no dutiable goods were manufactured in the factory other than exempted goods. The excise records of the assessee however, revealed that he was producing dutiable goods such as parts of locomotives, electric motors, etc., and hence exemption was not admissible on such waste and scrap. This resulted in incorrect grant of exemption of duty of Rs.12.45 lakh on the clearances of waste and scrap during the period 18 May 1995 to 30 September 1996.

This was pointed out in December 1996. Reply of the Ministry/department has not been received (November 1997).

iv) Parts of ship

As per a notification issued on 7 May 1977 (as amended), goods supplied as stores for consumption on board a vessel of the Indian Navy were exempted from payment of the whole of the duty of excise leviable thereon. The Board clarified in December 1988 that stores for consumption on board a vessel would cover consumable and non-consumable stores meant for use of a ship for running and maintenance as well as for crew members.

Two assessees, in Bolpur and Pune Commissionerate, manufactured main boiler pressure parts, gear boxes and appliances etc. and cleared them without payment of duty availing the exemption under the aforesaid notification. Test check of records revealed that these goods were not supplied to the Indian Navy for consumption as stores on board a vessel but were cleared to ship builders for construction of a new ship. Hence, exemption claimed was not in order. This resulted in incorrect grant of exemption of Rs.49.46 lakh between March 1993 and November 1996.

On this being pointed out (January 1994), the department contended (between February 1995 and February 1997) that maintenance of ship implied bringing it into operational order and that the notification did not contemplate that the supply of the goods should be directly from the factory of the manufacturer to Indian Navy vessels for use on board. So long as it could be shown that the goods had been supplied as stores and had been received for use on board a vessel of the Indian Navy, the substantive condition of the notification would be treated to have been met.

The reply is not tenable as the goods were procured by the ship builders for construction of a new ship. In the absence of the existence of a ship, the basic condition that the goods were used as stores on board a vessel of Indian Navy was clearly not satisfied.

Reply of the Ministry has not been received (November 1997).

v) **Blended products**

As per notification dated 1 March 1987, unprocessed cotton belting woven was chargeable to nil rate of duty. Under another notification dated 1 March 1994 as amended on 16 March 1995, cotton fabrics were exempt fully from excise duty.

The Supreme Court in the case of M/s. Rajasthan Spinning and Weaving Mills Limited {1995 (77) ELT 474} held that the exemption notification must be strictly construed and no extended meaning be given to the exempted item to enlarge its scope. Accordingly, it was decided that the exemption provided to polypropylene spun yarn was

not applicable to polypropylene blended yarn although both the products were classified under the same tariff item. It, therefore, follows that above exemption notifications were not applicable to blended cotton products of fabrics (cotton and flax) though both products were classifiable under the same tariff heading.

Two assessees, in Calcutta II Commissionerate, manufactured blended cotton fabrics (by using 67 per cent cotton and 33 per cent flax) and blended cotton belting (by mixing nylon hair with cotton). They cleared such blended products availing exemption under the aforesaid notifications. As the notifications were not applicable to blended cotton fabrics as per decision of the Supreme Court referred to above, the grant of exemption, was incorrect and resulted in short levy of duty of Rs.48.24 lakh between September 1988 and January 1996.

On being pointed out (November 1995 and June 1996), the department justified (January 1996 and March 1997) the grant of exemption on the ground that the exemption was allowed as cotton was predominant in the product. It further stated that the judgement of the Apex Court was not applicable as it related to the tariff which under went modification after introduction of new Tariff Act.

Reply of the department is not tenable as the rationale of the aforementioned judgement of the Supreme Court holds good in the facts and circumstances of the instant case and the principle laid down by the Apex Court had not been reversed.

Reply of the Ministry of Finance has not been received (November 1997).

vi) Plastic articles

As per notification dated 1 March 1988, as amended, films (other than of regenerated cellulose) were chargeable to concessional rate of duty and other plastic articles to 'nil' rate of duty if produced out of plastics in primary forms and plastic wastes falling under headings 39.01 to 39.15 on which the duty of excise had already been paid.

An assessee, in Chandigarh Commissionerate, was engaged in the manufacture of plastic films, tubings and other articles of plastic out of duty paid LDPE/HDPE granules. Duty paid on LDPE/HDPE granules was availed as Modvat credit and adjusted against duty payable on films, articles etc. During process of manufacture of above products, some waste and scrap were obtained which was stored and reprocessed into granules. These granules were used captively for the manufacture of films and plastic articles which were cleared, availing exemption under the aforesaid notification. Since no duty was paid on the waste and scrap or on granules, availment of exemption on films and plastic articles produced out of these reprocessed granules was incorrect and this resulted in short levy of duty of Rs.42.06 lakh from April 1990 to July 1993.

On this being pointed out (January 1994), the department contended that as the reprocessed granules had been manufactured out of waste and scrap of films, in the manufacture of which duty paid granules were used, the exemption availed was correct.

The reply of the department is not tenable as the assessee had already availed Modvat credit for the duty paid on inputs.

Reply of the Ministry has not been received (November 1997).

vii) Cement

According to a notification dated 16 March 1995, cement manufactured in a factory using rotary kiln with an installed capacity of 1,98,000 tonne per annum was chargeable to concessional rate of duty of Rs.200 per tonne. This concession was not applicable to cement bearing a brand name or trade name of another person.

As per the explanation under the notification, "'Brand name' or 'Trade name' shall mean 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 etc., which is used in relation to such specified goods for 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".

A mini cement factory 'X' in Guntur Commissionerate, availed the above concession on the cement manufactured by it, but marketed by another cement company 'Y', with the label on the bag "X cement marketed by 'Y' Limited". The concession was not available on the cement produced by X and marketed by Y in terms of the notification, ibid. The incorrect grant of exemption resulted in short levy of Rs.38.10 lakh during April 1995 to July 1996.

The Ministry contended (October 1997) that the words so used did not prevent the assessee from availing exemption.

Reply of the Ministry is not tenable as the use of such words clearly establishes connection in the course of trade of the product and the other company 'Y' limited and hence exemption was not admissible in terms of the explanation to the notification.

viii) Industrial oil

As per notification dated 16 March 1985, lubricants falling under heading 34.03 were chargeable to duty at 10 per cent ad valorem.

a) An assessee, in Calcutta I Commissionerate, manufacturing 'servo steelrol C-6' oil containing 42.64 per cent of mineral oils, was allowed to clear the product on payment of duty at 10 per cent ad valorem as per the above notification. A book published by the assessee on its products disclosed that the product was recommended for cold rolling of mild and medium carbon steel. Since the product was meant for use as rolling mill oil, the oil was a 'speciality oil' and not a lubricating preparation and hence exemption allowed was not correct. This resulted in short levy of duty of Rs.30.84 lakh during April 1995 to March 1996.

On being pointed out (August 1996), the department stated (March 1997) that a show cause notice demanding duty of Rs.30.84 lakh had since been issued on 25 March 1997.

Reply of the Ministry has not been received (November 1997).

b) Two assessees, in Mumbai II and III Commissionerates, manufactured textile treatment compound, textile treatment speciality compound, leather treatment compound, textile defoamer etc. and cleared them on payment of duty at 10 per cent ad valorem, under the above said notification, during 16 March 1995 to 22 July 1996. The products were used in the textile industry for treatment of textile materials and leather. Therefore, the products were not lubricating preparations and payment of duty at concessional rate of duty was not correct. This resulted in short levy of duty of Rs.23.66 lakh.

On being pointed out (October and November 1996), the department stated (November 1996) that demand notice was being issued in one case. Reply in the second case has not been received (November 1997).

Reply of the Ministry has not been received (November 1997).

ix) Paper

As per notification dated 1 March 1994, as amended, paper and paper board or articles made therefrom, falling under chapter 48, were chargeable to duty at 15 per cent ad valorem, provided that the said goods were manufactured, right from the stage of pulp, in the said factory and such pulp contained not less than 50 per cent by weight of pulp made from materials, other than bamboo, hard woods, soft woods, reeds (other than sarkanda) or rags.

An assessee, in Meerut Commissionerate, manufactured paper and paper board by using bamboo, wood and waste paper as raw materials and cleared them after availing exemption under the said notification. The excise records of the assessee, however, revealed that the percentage of pulp received from waste paper during April 1994 to August 1995 was less than 50 per cent by weight of pulp made from wood etc. The exemption availed was therefore, incorrect and resulted in short levy of duty of Rs.29.38 lakh.

On being pointed out (February 1996), the department contended (August 1996) that the scrutiny of records other than the excise records (Form IV and RT 5) showed that the percentage was above 50.

The reply is not acceptable because Form IV, RT-5 and RG 1 are the basic excise records which depict correct and true figures of raw materials consumed for manufacture and final product produced. Further, the detailed scrutiny of records of the assessee conducted by the Assistant Commissioner (July 1996) also revealed that the percentage of pulp received from waste paper was less than 50.

Reply of the Ministry has not been received (November 1997).

x) Thermo plastic polyethylene teraphthalate

As per notification dated 1 March 1994, as amended on 16 March 1995, full duty exemption was available to goods falling under heading 39.26, if no credit of duty paid on inputs used in the manufacture of such goods had been availed under rule 57A. It, therefore, follows that to be eligible for the exemption, the final products should have been manufactured using duty paid inputs, in respect of which no Modvat credit had been availed.

A 100 per cent export oriented unit, in Chennai Commissionerate, manufactured thermoplastic polyethylene terapthalate preforms and cleared it for home consumption on payment of basic customs duty but without payment of additional duty availing exemption under above notification dated 1 March 1994. As 100 per cent export oriented units get their inputs duty free, these units would not be eligible for the duty free concession in respect of additional duty levied in lieu of excise duty. Accordingly, there was short levy of additional duty of Rs.22.04 lakh during November 1995 to January 1996.

On being pointed out in June 1996, the department contended (July 1996) that the benefit could be extended to the assessee as they had not availed any input credit under rule 57A.

Reply of the department is not tenable as the assessee was not eligible for availing Modvat credit as none of the inputs utilised by the assessee had suffered duty, inputs required by such units being allowed duty free.

Reply of the Ministry has not been received (November 1997).

xi) Granulated slag

As per notification dated 1 March 1988 as amended on 25 July 1991, goods falling under chapter 26 were exempt from duty, provided no credit of duty paid on inputs used in the manufacture of goods had been taken under rule 57A of the Rules.

An assessee, in Calcutta II Commissionerate, manufacturing pig iron, was availing Modvat credit on various inputs used by him. The assessee also manufactured granulated slag falling under heading 26.18 during the course of manufacture of pig iron and cleared the granulated slag availing exemption under the said notification. Since Modvat credit was taken on the inputs, the grant of exemption was not correct. This resulted in short levy of duty of Rs.13.03 lakh during 1 December 1994 to 22 July 1996.

On being pointed out (March 1997), the department stated (April 1997) that slag was only a process waste and 1 per cent of slag waste consisted of oxides of the other trace elements of ores like iron, chromium, tin etc.

The reply of the department is neither relevant nor tenable in view of the restrictive clause in the notification. In a similar case featured in para 3.27 (ii) of the Audit Report 1991-92, the Ministry had accepted that in such a situation exemption would not be available.

7.3 Incorrect grant of exemption

As per notifications dated 25 July 1991 and dated 1 March 1994, concessional rate of duty at Rs.185 per tonne was leviable on cement produced by a cement factory using vertical shaft kiln with installed capacity not exceeding 66000 tonne per annum and factory using rotary kiln with installed capacity not exceeding 198000 tonne per annum.

The exemption was available subject to the production of certificate by an officer not below the rank of Director of Industries in the State Government or the Development Commissioner for cement in the Government of India.

A cement manufacturer, in Hyderabad Commissionerate, having a certificate of installed capacity of the factory as 66,000 tonne per annum for the year 1990-91 only, had availed the concessional rate of duty during the years 1991-92 to 1994-95. As the certificate obtained was relevant for the year 1990-91 only and did not mention the usage of kiln technology and further in view of the fact that the actual production of the factory was much higher than 66,000 tonne per annum in contravention of the limit as prescribed in the notification, the availment of concessional rate of duty by the assessee was inadmissible. This resulted in short levy of duty of Rs.5.39 crore during 1991-92 to 1994-95.

On being pointed out (July 1995), the Ministry stated (July 1997) that the assessee was using rotary kiln and hence exemption availed was correct.

The reply is not tenable as neither the assessee nor the department could produce requisite certificate for the relevant period from the competent authority. Further, the certificate obtained on 22 July 1995 from Commissioner of Industries did not indicate the use of any specific type of kiln and hence was not valid for the purpose of granting exemption.

7.4 Incorrect exemption on the basis of defective notification

As per serial No.1 of the table to notification dated 16 March 1995, effective rate of duty, for floor coverings excluding jute carpets falling under chapter 57, was 30 per cent ad valorem while for the floor coverings of jute falling under the same chapter, the duty was 5 per cent ad valorem vide serial No.3. It follows that 'jute carpets' being specifically excluded from serial No.1 were chargeable to duty at 5 per cent and other floor coverings of jute were liable to duty at 30 per cent ad valorem under serial No.1 of the said notification.

An assessee, in Calcutta II Commissionerate, was allowed to clear jute mattings on payment of duty at the rate of 5 per cent ad valorem. This was not correct as 'jute mattings' were not excluded from levy of 30 per cent ad valorem and jute mattings and jute carpets were different products. Therefore, payment of duty at 5 per cent ad valorem instead of 30 per cent ad valorem was incorrect thereby resulting in short realisation of duty of Rs.1.14 crore during 16 March 1995 to 30 June 1996.

On being pointed out (January 1997), the department contended (January 1997) that jute mattings were neither specifically excluded from serial No.3 nor included in serial No.1 and hence payment of duty at 5 per cent ad valorem was correct.

The department's contention is not acceptable as jute carpets being specifically excluded, other floor coverings of jute stood contained in serial No.1 of the notification.

Reply of the Ministry has not been received (November 1997).

7.5 Incorrect grant of exemption on goods used within the factory of production

i) As per notification dated 16 March 1995, goods falling under chapters 72, 73, 82, 83, 84 or 85 other than (a) electrical stampings and lamination, (b) bearing and (c) winding wires, were exempt from duty if the said goods were used within the factory of production in the manufacture of specified power driven pumps.

An assessee, in Mumbai I Commissionerate, engaged in the manufacture of power driven pumps manufactured winding wires which was then captively consumed without payment of duty under the aforesaid notification, for manufacture of electric motors, which in turn was used in the manufacture of power driven pumps. As exemption was not available to winding wires, grant of exemption was incorrect and resulted in short recovery of duty of Rs.1.04 crore during January 1996 to November 1996.

This was pointed out in January 1997. Reply of the Ministry/department has not been received (November 1997).

ii) As per notification dated 2 April 1986, specified goods manufactured in a factory and used as inputs in the manufacture of specified final products were exempt from payment of duty provided the said final products were not exempt from duty or were not chargeable to nil rate of duty.

Two assessees, in Mumbai I and III Commissionerates, manufactured fuel gas, transmission shafts, parts of motor vehicles etc. and used them captively without payment of duty in the manufacture of final products which were also exempt from payment of duty. This resulted in incorrect grant of exemption of Rs.48.90 lakh between September 1991 and July 1996.

On being pointed out (August 1995 and February 1996), the department stated (May and September 1996) that one assessee had paid Rs.5.85 lakh on fuel gas consumed during November 1995 to April 1996 and show cause notices were being issued for recovery of the remaining duty Rs.43.05 lakh from both the assessees.

Reply of the Ministry has not been received (November 1997).

7.6 Incorrect grant of exemption on goods manufactured by a job worker

As per notification dated 25 March 1986, as amended, specified goods manufactured in the factory on job work and used in or in relation to manufacture of final products (on which duty of excise was leviable whether in whole or in part) were exempt from the whole of duty leviable thereon.

An assessee, in Calcutta I Commissionerate, removed raw materials/semi-finished goods to different job workers for processing, fabrication, manufacturing etc., without payment of duty under the said notification and got it back from the job workers after such processing. The said processed goods were used in the manufacture of railway wagons. Since the final products viz., railway wagons were exempt, the exemption was not available and duty of Rs.29.73 lakh on such processed goods was leviable from April 1995 to January 1997.

On being pointed out (January 1997), the department contended (February 1997) that notification dated 25 March 1986 did not stipulate any such condition that the final products should be dutiable.

The department's contention is factually incorrect as leviability of duty on final products is the main condition of the notification.

Reply of the Ministry has not been received (November 1997).

7.7 Incorrect grant of exemption on the basis of rescinded notification

Two assessees, in Ahmedabad Commissionerate, manufacturing wires of iron and non-alloy steel falling under sub-heading 7217.90, cleared their products between April 1994 and March 1996 without payment of duty claiming exemption under notification dated 20 May 1988 which was rescinded on 1 March 1994. Grant of exemption on the basis of notification already withdrawn, resulted in short levy of duty of Rs.24.09 lakh during April 1994 to March 1996.

This was pointed out in July 1996. Reply of the Ministry/department has not been received (November 1997).

7.8 Other cases

In 7 other cases of incorrect grant of exemption, the Ministry/department, while accepting short levy of duty of Rs.47.35 lakh, reported recovery of Rs.12.45 lakh till November 1997.

8. VALUATION OF EXCISABLE GOODS

A wide range of the excisable commodities are leviable to ad valorem rates of duty. The valuation of excisable goods is governed by section 4 of the Central Excise Act, 1944, read with the Central Excise Valuation Rules, 1975.

Some of the illustrative cases of short levy due to undervaluation are mentioned below:

8.1 Additional considerations not included in the assessable value

According to section 4 of the Act, the normal price at which such goods are sold ordinarily by the assessee to a buyer in the course of wholesale trade for delivery at the time and place of removal would be the assessable value provided the price is the sole consideration for sale. In cases, where price is not the sole consideration, the assessable value of the goods, as per the provisions of rule 5 of Valuation Rules, shall be based on the aggregate of the price and money value of additional considerations flowing directly or indirectly from the buyer to the assessee.

i) Realisation of retail pump outlet charges etc.

The Supreme Court in the case of M/s. Bombay Tyre International {1983 ECR 1627 D (SC)} held that the expenses incurred on account of the several factors which have contributed to the value of the product upto the date of sale, which apparently would be the date of delivery, are liable to be included in the assessable value of the product.

The Board in it's circular dated 21 June 1996 also clarified that the amount collected by the oil companies in the form of state surcharges, retail pump outlet (RPO) charges/surcharges, railway siding/shunting charges and air field charges from the buyer on the sale of petroleum products are includible in the assessable value.

Twenty five units of four public sector oil corporations (Bolpur (1), Bangalore (1), Bhubaneswar (2), Calcutta I (7), Calcutta II (4), Chandigarh (1), Chennai (1), Delhi (1),

Guntur (1), Madurai (1), Mumbai II (1), Mumbai III (1), Patna (2) and Trichy (1) Commissionerates), cleared petroleum products falling under chapter 27 recovering charges such as RPO charges/surcharges, state surcharges, railway siding charges, shunting charges, railway/road freight from the buyers on the invoice values. Non-inclusion of these items in the assessable value resulted in undervaluation of the goods and consequent short levy of duty of Rs.14.05 crore during March 1994 to March 1997.

On being pointed out (between March 1995 and July 1997), the department intimated (between August 1996 and June 1997) that in six cases show cause notices for Rs.6.05 crore were either issued or were under issue. In two cases, it contended that such charges were not includible as the price of the product was fixed by the Ministry of Petroleum. In the remaining seventeen cases, reply has not been received (November 1997).

Reply of the department is not tenable in view of Supreme Court's decision of 1983 and Board's clarification of June 1996.

Reply of the Ministry has not been received (November 1997).

ii) Interest

a) Interest on deposit

The Ministry clarified on 13 June 1990 that interest accrued on advance deposits made by customers should be included in the assessable value of the products since the manufacturer would have incurred liability to pay interest, had he borrowed the amount from banks and therefore, it was not necessary to establish separately the nexus between the deposits and the price.

Supreme Court of India in the case of Metal Box (India) Limited {1995 (75) ELT 449} also upheld the above view (January 1995) and decided that the notional interest on advances made by customers to assessee is to be added to arrive at the assessable value.

Seven assessees (Bangalore (1), Calcutta I (1), Chandigarh (1) Hyderabad (2), Mumbai I (1) and Pune (1) Commissionerates), engaged in the manufacture of different excisable goods collected deposits/advances but interest accrued thereon was not included in the assessable value. This resulted in undervaluation of goods and consequent short levy of Rs.1 crore between March 1991 and June 1996.

On being pointed out (between December 1992 and December 1996), the department admitted the audit objection in three cases and in the other three cases, it intimated that show cause cum demand notices were under issue. In the remaining one case, it contended (October 1993) that the High Court of Madras in the case of Laxmi Machine Works Limited had held that the interest factor would be relevant only to the extent actual benefit was gained from the advances.

The contention of the department is not tenable in view of the fact that the assessee had received an amount of Rs.23.69 crore interest free advance and utilised it as working capital. The department had not worked out the benefit obtained by the assessee in terms of the judgement of the Madras High Court.

Reply of the Ministry has not been received (November 1997).

b) Interest on finished goods

The Supreme Court in the case of M/s. Madras Rubber Factory Limited {1995 (77) ELT 433} held that interest on finished goods lying in stock is not excludible from the assessable value.

An assessee, in Calcutta I Commissionerate, manufacturing electric fans paid duty on the assessable value arrived at after deducting element named as "interest on bill" from the wholesale price. This interest on bill was nothing but an interest on finished goods lying in stock. This resulted in undervaluation of goods and consequent short levy of duty of Rs.24.88 lakh during April 1994 to September 1996.

On being pointed out (November 1996), the department contended (June 1997) that the assessee had not claimed any deduction on interest on bill.

Reply of the department is not based on facts as assessee had infact reduced the assessable value, by the amount of interest on bill.

Reply of the Ministry has not been received (November 1997).

iii) Value of waste/scrap retained

An assessee, in Mumbai II Commissionerate, manufactured mild steel drums, out of the raw materials supplied by the buyer and cleared them on payment of duty. A scrutiny of the contract and price list showed that the assessee was allowed to retain scrap, rejections, residue etc., generated during the process of manufacture of the goods and the assessable value was arrived at, after taking cost of sheet used in the manufacture of drums and not the gross quantity of sheet supplied. The additional consideration received in the form of sale proceeds of waste and scrap, was not included in the assessable value of the final products. This resulted in short levy of duty of Rs.29.30 lakh between August 1992 to March 1996.

On being pointed out (August 1994), the department contended (November 1995) that the scrap generated became the property of the assessee by virtue of the contract.

The reply of the department is not acceptable because the value of sale proceeds of the scrap was an additional consideration which was required to be included in the assessable value of the finished goods.

Reply of the Ministry has not been received (November 1997).

iv) Escalation charges

According to the circular of the Board dated 4 October 1980, in the case of running contracts, where there is a price variation clause, the goods should be provisionally assessed at the time of clearance and final assessment be made as soon as

the assessee submits his bills for the escalated value, without waiting for their acceptance by the customers.

Four assessees, (Aurangabad (2), Calcutta II (1) and Mumbai III (1) Commissionerates), manufacturing various excisable goods, raised demands on the customers for escalation of prices but duty due was not paid. This resulted in short levy of Rs.25.23 lakh between April 1993 and October 1996.

On being pointed out (between May 1995 and January 1997), the Ministry/department, while accepting objection reported recovery of Rs.18.73 lakh in three cases and issue of show cause cum demand notice for Rs.6.50 lakh in one case (between July 1996 and December 1997).

8.2 Inadmissible deductions allowed from assessable value

As per section 4(4)(d)(ii) of the Act, 'value' in relation to any excisable goods does not include trade discount allowed in accordance with the normal practice of wholesale trade.

i) Dealer's commission

The Supreme Court in the case of M/s. Coromandal Fertilizer Limited {1984 (17) ELT 607} held that commission paid to selling agents is not a trade discount within the meaning of explanation to section 4 of the Act, and does not qualify for deduction.

Five assessees, (Bangalore (1), Chandigarh (2), Delhi (1) and Jamshedpur (1) Commissionerates), engaged in the manufacture of tractors, motor cycles, mopeds, circuit breakers etc., were selling their products through the authorised dealers and were allowing commission to them from wholesale price. Such dealer's commission was provided to meet "after sales service charges", "cost of promotion of sales", "cost of processing orders", "publicity and advertising expenses" etc. The commission was not a permissible deduction and was, therefore, includible in the assessable value of the products, which was

not done. This resulted in short levy of duty of Rs.3.27 crore during April 1993 to June 1996.

On being pointed out (between August 1995 and October 1996), the department admitted (between November 1995 and February 1997) objection in two cases. In the third case show cause notice was stated to be under issue. In the remaining two cases, it contended that duty was leviable on the prices at which the goods were sold by the assessees and not by the dealer as the dealer's commission did not flow back to the assessees.

The reply is not tenable in view of the Supreme Court judgement cited above.

Reply of the Ministry has not been received (November 1997).

ii) Transportation and insurance charges

The Ministry in its circular dated 25 April 1988 clarified that the actual expenses on account of transportation of finished goods from the place of removal to the place of delivery is a permissible deduction from assessable value.

Six assessees, (one each in Chandigarh, Chennai, Cochin, Delhi, Meerut and Nagpur Commissionerates), engaged in the manufacture of cosmetic articles, pan masala leather garments, yarn, pipes, poles etc., were claiming deduction on transportation and insurance charges from assessable value of their products. Accounts of the assessees showed that the actual expenditure incurred on freight and insurance was less than the deduction claimed by the assessees. Allowance of excess deduction, resulted in undervaluation of goods and consequent short levy of duty of Rs.40.07 lakh between April 1988 and December 1996.

On being pointed out (between April 1995 and March 1997), the Ministry/department admitted audit objection (between March and September 1997) and intimated recovery of Rs.18.98 lakh in four cases and confirmation of demand of Rs.2.45

lakh in the fifth case. Reply of the Ministry in the sixth case has not been received (November 1997).

iii) Distribution charges

The Supreme Court in the case of M/s. Bombay Tyre International held in October 1983 that the expenses incurred on account of the several factors which have contributed to the value of the product upto the date of sale are liable to be included in the assessable value. This was reinforced by the judgement of the Supreme Court in the case of Madras Rubber Factory Limited {1993 (77) ELT (433)} which held that the expenses incurred in maintaining and running the sale depots cannot be deducted from the assessable value.

Two assessees in Calcutta II and Jamshedpur Commissionerates, engaged inter-alia in the manufacture of iron and steel products cleared the products to the depots of the buyers at the price determined by the buyers. However, duty was paid on the assessable value arrived at after deducting "distribution charges" at the rate ranging from Rs.500 to Rs.600 per tonne from the price. Inadmissible deduction, resulted in short levy of duty of Rs.20.90 lakh during April 1994 to July 1995.

On being pointed out (January 1996), the Ministry admitted (June and December 1997) the audit objection.

8.3 Non-inclusion of pre-manufacturing expenses

The Supreme Court in the case of M/s. Bombay Tyre International held in October 1983 that the expenses incurred on account of the several factors which have contributed to the value of the product upto the date of sales are liable to be included in the assessable value. The Tribunal in the case of M/s. Thermax (P) Limited {1994 (70) ELT 247} further clarified that in the case of goods to be installed at site of the customer, designing, engineering, erection and commissioning charges are includible in the assessable value.

Three assessees, in Ahmedabad, Chennai and Hyderabad Commissionerates, manufactured lifts, EPABX apparatus, radio equipments and control system etc., on

contract basis, for assembly at site. Though assessees recovered full value of the products assembled at site inclusive of designing/engineering/installation/commissioning charges and value of bought out items on separate invoices, they did not include such charges and cost of bought out items in the assessable value. This resulted in undervaluation of goods and consequent short levy of duty of Rs.4.14 crore between September 1988 to May 1992.

On being pointed out (between April 1992 and February 1995), the department confirmed (August 1996) duty of Rs.24 lakh in one case. In the remaining two cases, it contended that value of bought out items as well as installation and commissioning charges etc., were not includible in the assessable value as they were in the nature of post manufacturing expenses.

Reply of the department is not tenable because the manufacture of the products in question was complete only when they were installed/commissioned and hence value of such charges was includible in the assessable value.

Reply of the Ministry has not been received (November 1997).

8.4 Non-inclusion of duty paid on inputs in the assessable value

The Supreme Court, while discussing the validity of section 4(4)(d)(ii) in the case of M/s. Kirloskar Brothers Limited {1992 (59) ELT 3}, held that abatement for excise duty is allowable only for the duty payable on the goods to be assessed and not for the duty already paid on the inputs.

Fourteen assessees, in Ahmedabad, Allahabad, Bangalore, Bhubaneswar, Belgaum, Calcutta I and II, Chandigarh, Jaipur (2), Kanpur, Meerut, Shillong and Surat Commissionerates, engaged in the manufacture of different excisable products, took Modvat credit of duty paid on the inputs used in the manufacture of their final products. The goods manufactured by the assessees were cleared on payment of duty on the assessable value arrived at incorrectly, after excluding the duty paid on the inputs. This resulted in short levy of duty of Rs.3.39 crore between April 1993 and February 1997.

On being pointed out in audit (between March 1995 and May 1997), the Ministry admitted (October 1997) the audit objection in one case. Reply, in the remaining thirteen cases, has not been received (November 1997).

8.5 Valuation of goods manufactured on behalf of others

According to section 4 of the Act, the assessable value should be the normal price at which goods are sold in the wholesale trade. Further, Supreme Court of India in the case of Bombay Tyre International {1983 (44) ELT 1896} have held that selling, distribution and advertisement expenses should be included in the assessable value of goods.

Three assessees, two in Bangalore and one in Nagpur Commissionerates, engaged in the manufacture of scouring powder and medicines, entered into agreement with other companies for manufacture and supply of final products under their brand names. According to the terms of agreement, the assessee would supply the products according to the despatch instructions by the brand name owners all marketing and selling operations of the product were to be undertaken by the buyer companies, the entire production was to be cleared to the buyer companies on the value agreed between them and the assessee company had no right to sell the products directly to any other customer. All these conditions establish that the assessees were not independent manufacturers but only manufacturing the branded goods on behalf of the buyer companies. Therefore, the assessable value of the product should have been the value at which the buyer companies cleared the goods in the wholesale trade. This resulted in undervaluation of goods and consequent short levy of duty of Rs.2.39 crore during April 1994 to June 1996.

This was pointed out in audit (August and October 1996). Reply of the Ministry has not been received (November 1997)

8.6 Valuation of goods consumed captively

Where excisable goods are wholly consumed within the factory of production or in any other factory of the same manufacturer, the assessable value is to be determined

under section 4(1)(b) of the Act, read with Valuation Rules, on the basis of value of comparable goods or cost of production including a reasonable margin of profit, if value of comparable goods is not ascertainable.

i) Value of inputs

Four assessees, (Delhi (1) Mumbai II (1) and III (2) Commissionerates), engaged in the manufacture of plastic goods, blended lubricants, electrical goods, etc., cleared input goods as such or after subjecting them to certain manufacturing processes to their sister units for captive consumption. The value of goods so cleared for captive consumption was adopted at a lower rate than the actual cost. This resulted in undervaluation of finished goods and consequent short levy of Rs.1.19 crore between April 1994 and May 1996.

On being pointed out (between July 1995 and August 1996), the Ministry/department admitted audit objection and intimated (between November 1996 and June 1997) recovery of Rs.1.03 crore in three cases. Reply in the fourth case has not been received (November 1997).

ii) Value of intermediate goods

Ten assessees, (Ahmedabad (1), Chennai (2), Indore (1), Mumbai III (3), Pune (1) and Raipur (2) Commissionerates), engaged in the manufacture of various goods had cleared the goods for captive consumption on payment of duty on the assessable value arrived at on cost basis which was lower than the actual cost. This resulted in short payment of duty of Rs.61.02 lakh during April 1989 to July 1996.

On being pointed out (between July 1993 and January 1997), the Ministry/department admitted (between June 1995 and December 1997) audit objection and recovered Rs.63.67 lakh.

iii) Element of profit

The High Court of Punjab and Haryana held, in the case of M/s. Food Specialities Limited {1986 (33) ELT 331} that for captive consumption, notional profit at the rate of 10 per cent may be added to the cost, while arriving at the assessable value on cost basis, in cases were actual profit was not ascertainable.

Six assessees, (Coimbatore (2), Chandigarh (1), Kanpur (1), Meerut (1) and Mumbai I (1) Commissionerates), manufactured different products and consumed them captively in the manufacture of finished goods either in their own factories or in the factory of sister concerns. While determining the assessable value on cost basis, profit margin was adopted less than the actual profit and where actual profit was not known, the notional profit included was less than ten per cent. Non-inclusion of correct profit element in the assessable value resulted in short levy of duty of Rs.60.41 lakh between April 1991 and March 1996.

On being pointed out (between March 1993 and January 1997), the department admitted (between July 1996 and March 1997) audit objection in five cases and intimated recovery of Rs.32.16 lakh. In one case, it contented (March 1996) that there was no loss of revenue as duty paid on inputs would be available as Modvat credit for adjustment against duty payable on outputs.

Reply of the department is not relevant as products were not correctly assessed.

The Ministry confirmed the facts in one case (September 1997). Reply in the remaining four cases has not been received (November 1997).

8.7 Cost of components/raw materials supplied by buyer not included

Four assessees, in Chennai (1), Calcutta II (1), Mumbai II (1), and Mumbai III (1) Commissionerates, manufacturing 'depression chamber assembly', axle front, stopper, drum, sodium, petroleum sulphonate, etc. obtained components or raw materials free of cost from the buyer of the said products. The assessee paid duty on assessable value of

the finished goods arrived at after excluding the cost of components or raw materials obtained from the buyers. Non-inclusion of the cost of such components/raw materials in assessable value, resulted in short payment of duty of Rs.1.15 crore during March 1993 to August 1996.

On being pointed out (between June 1996 and January 1997), the Ministry/department intimated (March 1997) the recovery of Rs.98.95 lakh in two cases. Reply of the Ministry in the remaining two cases has not been received (November 1997).

8.8 Incorrect declaration of assessable value

An assessee, in Chennai Commissionerate, engaged in the manufacture of pesticides at Ennore cleared goods in bulk form to his own factories at Ambattur and Velachery for packing these products in smaller packings and for sale through it's depots. The assessee, however, paid duty by adopting the bulk stage price, notwithstanding the fact that the higher wholesale price at the depot was very much available and there were no sales at the factory gate. Payment of duty at lower assessable value resulted in short levy of duty of Rs.51.21 lakh between September 1995 and January 1996.

On being pointed out (February 1996), the department stated (February 1997) that a demand of Rs.51.21 lakh has been confirmed on the assessee.

8.9 Non-inclusion of shrinkage value of fabrics

Assessable value of processed fabrics under job work is the sum total of the value of grey fabrics, job charges and profit as decided by the Supreme Court in the case of M/s. Ujagar prints {1988 (19) ECR 578 (SC)}.

An assessee, in Calcutta II Commissionerate, received grey fabrics from various cloth merchants for processing. During processing, 4 to 5 per cent of grey fabric was shrinking. However, the processed fabrics, was allowed to be cleared on payment of duty on the length and value of the processed fabrics without adding the element of shrinkage.

The incorrect computation of assessable value, resulted in short levy of duty of Rs.47.79 lakh during June 1991 to October 1996.

On being pointed out (December 1995 and March 1997), the Ministry admitted (December 1996) the objection and intimated issue of show cause cum demand notice for Rs.46.91 lakh.

8.10 Other cases

In twelve other cases, the Ministry/department while accepting short levy of duty of Rs.107.79 lakh, reported recovery of Rs.72.03 lakh till November 1997.

9. MODVAT SCHEME ON INPUTS

Under Modvat scheme, credit is allowed for duty paid on specified inputs for manufacture. This credit can be utilised towards payment of duty on outputs, subject to fulfillment of certain conditions.

Some of the cases where incorrect availment of credit was noticed in audit are mentioned below:

9.1 Availment of credit without valid duty paying documents

As per proviso below rule 57G(2) of the Rules, no credit of duty paid shall be taken unless the inputs are received in the factory under documents like an invoice issued by a manufacturer of inputs under rule 52A, an AR-1, application for removal of excisable goods or triplicate copy of bill of entry etc., evidencing the payment of duty on such inputs.

As per rule 52 A (6) and (7) of the Rules, invoices used for delivering goods from a factory or a warehouse should bear printed serial numbers and should be authenticated by the owner, or working partner or Managing Director/Company Secretary as the case may be.

i) An assessee, in Jamshedpur Commissionerate, availed Modvat credit on sheet bar on the strength of 'despatch advice' (inter plant transfer) issued by another assessee. Since despatch advice was not a prescribed document, Modvat credit availed of Rs.3.66 crore during April to July 1994 was not in order.

On being pointed out (October 1995), the department contended (February 1997), that 'inter plant transfer advice' was permitted as a duty paying document in lieu of 'gate passes' within the meaning of rule 52A. Reply is not tenable since 'inter plant transfer advice' was not prescribed as a document for claiming Modvat benefit under rule 57G. Further, the reply of the department is contradictory to its own order dated 2 December

1992 clarifying that the 'inter plant transfer advice' was not a valid document for taking Modvat.

Reply of the Ministry has not been received (November 1997).

ii) An assessee, in Vadodara Commissionerate, availed credit of Rs.1.83 crore based on invoices which were not authenticated by the owner or did not bear printed serial numbers. The credit of Rs.1.83 crore availed during August 1995 to July 1996 was, therefore, incorrect.

On being pointed out (September 1996), the department contended (August 1997) that the credit should not be denied because the invoices were not authenticated or serial numbers were not printed. However, the department subsequently issued show cause notices for Rs.2.70 crore for the period July 1995 to August 1996.

Reply of the department is not tenable since such documents were not valid duty paying documents for claiming Modvat credit in view of specific provisions of rules 57G(2) and 52A(6).

Reply of the Ministry has not been received (November 1997).

iii) An assessee, in Mumbai III Commissionerate, availed Modvat credit of Rs.83.58 lakh on the invoices issued under rule 100E for clearing goods within the country by a hundred per cent export oriented unit. Availment of credit on the basis of documents not specified under rule 57G(2), resulted in incorrect availment of Modvat credit of Rs.83.58 lakh during July, October and November 1995.

This was pointed out in March 1997; reply of the Ministry/department has not been received (November 1997).

iv) Thirty two assessees, in seventeen Commissionerates, availed/utilised Modvat credit of Rs.1.31 crore on the basis of hand written/stamped invoices, commercial invoices, invoices marked 'not for sale', delivery challans, debit memos, documents not in the name of assessees, xerox copies of documents etc. As these documents were not

valid duty paying documents, grant of credit of Rs.1.31 crore between February 1994 and July 1996 was incorrect.

On being pointed out (between September 1994 and March 1997), the Ministry admitted the objection in seven cases. Reply in the remaining cases has not been received (November 1997).

(v) Two manufacturers of plastic woven bags and synthetic yarn, in Jaipur and Hyderabad Commissionerates, were allowed to avail Modvat credit of Rs.21.55 lakh between March 1994 and February 1996 though the inputs were received without duty paying documents. The availment of credit of Rs.21.55 lakh was, therefore, incorrect.

On being pointed out (August and September 1996), the Ministry intimated (November 1997) recovery of Rs.3.22 lakh in one case. Reply in the second case has not been received (November 1997).

9.2 Modvat credit availed in excess of the admissible amount

i) According to rule 57A read with the notification issued thereunder, the Modvat credit of additional duty paid under section 3 of the Customs Tariff Act, 1975, shall be admissible to the extent of duty of excise leviable on such goods.

An assessee, in Mumbai III Commissionerate, paid additional duty at the rate of 10 per cent ad valorem on imported iron ore pellets (heading 26.01) and availed credit of Rs.4.58 crore during September to November 1996. Since iron ore pellets were leviable to excise duty at nil rate under notification dated 23 July 1996 availment of Rs.4.58 crore as credit was not in order.

This was pointed out in January 1997; reply of the Ministry/department has not been received (November 1997).

ii) Ten assessees, (Bangalore (1), Chennai (6), Pune (1) and Trichy (2) Commissionerates), engaged in the manufacture of various goods, availed credit in excess

of the duty actually paid by them on inputs. This resulted in excess availment of credit of Rs.22.79 lakh during January 1993 to October 1996.

On being pointed out (between March 1994 and December 1996), the department admitted the objection and reported recovery of Rs.22.79 lakh.

The Ministry admitted the objection in five cases (August and October 1997). Reply in the remaining five cases has not been received (November 1997).

9.3 Short reversal of credit by VABAL licencees

According to clause V of Customs notification dated 19 May 1992, Modvat credit is not admissible on inputs/raw material used in the manufacture of goods to be exported under the value based advance licensing scheme. However, the Ministry subsequently, vide its circular dated 10 January 1997, allowed reversal of Modvat credit availed in contravention of the value based advance licensing scheme provided interest at 20 per cent per annum is paid on belated reversal.

An assessee, in Mumbai III Commissionerate, engaged in manufacture of goods exported partially oriented yarn (POY) and polyester staple fibre (PSF) under the value based advance licences (VABAL) scheme. Although Modvat credit of duty paid on inputs was not admissible to the assessee as he was availing benefits under VABAL scheme, yet he availed of the benefit of Modvat credit on various inputs and later reversed the credit. Test check of reversal of credit in respect of two inputs alone (purified teraphthalic acid and monoethylene glycol) showed that the credit of Rs.3.32 crore was reversed as against the credit of Rs.5.88 crore which was required to be reversed. This resulted in short reversal of credit of Rs.2.56 crore during May 1992 to July 1994 in respect of two inputs alone. Short reversal of credit similarly in respect of other inputs was suggested to be worked out by the Commissionerate. The delayed reversal would also call for levy of interest which upto June 1997 worked out to Rs.2.05 crore (approximately) in case of two inputs test checked in audit.

The omission was pointed out in audit in January 1996; reply of the Ministry/department has not been received (November 1997).

9.4 Availment of credits on inputs used in exempted output

As per rule 57C of the Rules, no credit of duty paid on the inputs used in the manufacture of final products shall be allowed, if the final product is exempt from whole of the duty of excise leviable thereon or is chargeable to nil rate of duty.

Twenty five assessees, in twelve Commissionerates, engaged in the manufacture of various excisable goods availed Modvat credit of Rs.2.20 crore on inputs which were used in the manufacture of exempted goods or goods cleared at nil rate of duty. This resulted in incorrect availment of Modvat credit of Rs.2.20 crore during the period September 1991 to January 1997.

On being pointed out (between July 1994 and January 1997), the department admitted objection in all the cases and intimated recovery of Rs.1.36 crore till November 1997.

Acceptance of the Ministry had been received (November 1997) in four cases.

9.5 Availment of credit on goods not covered under the Modvat scheme

i) Packaging material

As per explanation below rule 57A of the Rules, input does not include packaging materials, the cost of which is not included or had not been included during the preceding financial year, in the assessable value of the final product.

Two assessees, in Bangalore Commissionerate and one assessee in Cochin Commissionerate, availed Modvat credit of Rs.90.42 lakh of duty paid on glass bottles, corks etc., and utilised such credit for payment of duty on aerated waters, between July

1991 and December 1996. Since the value of the bottles/corks was not included in the assessable value of the final product, availment of credit was clearly not in order.

On being pointed out (between September 1993 and February 1997), the Ministry admitted the objection in one case and added (August 1997) that while duty of Rs.18.70 lakh for the period from April 1994 to September 1995 had been recovered, demand for the period prior to April 1994 was not raised as goods were chargeable to specific rate of duty. Reply is not relevant as there was a clear contravention of the provisions of rule 57A. Reply in the remaining two cases has not been received (November 1997).

ii) Petroleum oils

Two assessees, in Vadodara and Surat Commissionerates, were allowed to avail Modvat credit of Rs.40.72 lakh on petroleum oils falling under sub-heading 2710.12. Since such petroleum oils are not covered under the Modvat scheme, availment of credit of Rs.40.72 lakh during May 1994 to January 1997, was incorrect.

On being pointed out (February and March 1997), the department intimated (March 1997) recovery of Rs.40.72 lakh.

Reply of the Ministry has not been received (November 1997).

iii) Lubricating oil and greases

Two assessees, in Bolpur and one in Calcutta II Commissionerate, availed and utilised Modvat credit on "lubricating oil and lubricating grease". These goods were used merely for the better operation of machinery and were not used as input in or in relation to the manufacture of final product and hence availment of Modvat credit of Rs.32.31 lakh during April 1994 to January 1997 was not in order.

On being pointed out (between July 1995 and February 1997), the department admitted objection in one case and stated (April 1997) that Modvat credit on such goods was clearly disallowable. In the second case, it contended (March 1997) that Modvat credit on such goods was allowable as goods were used in or in relation to the

manufacture of final products while in the third case it contended that Modvat credit was admissible under rule 57Q (credit of duty paid on capital goods) as products were used to run the machinery.

Reply of the department is not tenable since the goods were not used as input. Further CEGAT in the case of M/s. Kanoria Sugar and General Manufacturing Company Limited {1996 (87) ELT 522} specifically decided that lubricating oil and lubricating grease would not qualify as input under rule 57A. Further, such products do not also qualify under the definition of capital goods and hence credit is also not admissible under rule 57Q.

Reply of the Ministry has not been received (November 1997).

iv) Grey cloth

As per notification dated 21 October 1994, grey cloth falling under heading 51.06 has been specified as an input for the manufacture of woollen fabrics (heading 51.07).

An assessee, in Chandigarh Commissionerate, availed Modvat credit of Rs.35.18 lakh paid on woollen yarn (heading 51.03) and utilised the same towards payment of duty on finished woollen cloth. Records of the assessee showed that woollen yarn was used in the manufacture of grey cloth which in turn was used in the manufacture of finished woollen cloth. Since grey cloth was not an input specified under rule 57A till 20 October 1994 and was exempt from duty, availment of Modvat credit of Rs.35.18 lakh, on woollen yarn from July to September 1994, was incorrect.

On being pointed out (July 1995), the department contended (June 1996) that non-specification of the grey cloth under rule 57A was immaterial as it was not marketable.

The reply of the department is not tenable as grey cloth was marketable and was specified as an input from 21 October 1994 only.

Reply of the Ministry has not been received (November 1997).

v) **Transformer oil**

As per CEGAT's decision in the case of M/s. NGEF Ltd., {1995 (77) ELT 238 (T), transformer is an electrical equipment and its manufacture can be said to be complete, the moment all the electrical components for conversion of the voltage are in place. Thus, transformer oil not filled in the transformer before its clearance but merely sent alongwith transformer cannot be considered as a component of transformer.

An assessee, in Mumbai II Commissionerate, availed Modvat credit on transformer oil which was not filled in the transformer at the time of clearances of the transformers but was cleared separately. Since the goods were not used for manufacture of the final product, it could not be treated as input and did not qualify for availment of Modvat credit. Therefore, availment of Modvat credit on transformer oil cleared separately during the year 1994-95 to 1996-97 was, not in order.

On being pointed out in March 1997, the department intimated (May 1997) that draft show cause cum demand notice for an amount of Rs.49.34 lakh for the period from March 1994 to June 1995 was under issue by the Commissioner.

Reply of the Ministry has not been received (November 1997).

9.6 Availment of credit beyond prescribed period of six months

According to second proviso to rule 57G(2) as inserted on 29 June 1995, credit of duty paid on inputs shall not be admissible after six months of the date of issue of specified duty paying documents.

i) An assessee, in Surat Commissionerate, incorrectly availed Modvat credit after six months on 28 September 1995 amounting to Rs.47.55 lakh being duty paid on imported aluminium scrap based on bills of entry (specified duty paying document) issued on 22 and 23 February 1995.

On being pointed out (February 1996), the Ministry contended (June 1997) that the period of six months was to be counted from the date of actual receipt of goods in the

factory. It further contended that the said proviso of rule 57G(2) was not applicable as duty paying documents were issued prior to its insertion in rule 57G.

Reply of the Ministry is contradictory to the said clear provisions of rule 57G(2). Further, these provisions were applicable in this case as credit was availed after its insertion in the rule.

ii) Twenty nine assessees, in thirteen Commissionerates, engaged in the manufacture of various excisable goods availed Modvat credit of duty on inputs after a lapse of six months from the date of issue of the specified duty paying documents, between July 1995 and December 1996. The availment of credit after the stipulated period of six months, resulted in an incorrect availment of Modvat credit of Rs.1.47 crore.

On being pointed out (between November 1995 and March 1997), the department admitted the objection in thirteen cases and reported issue of show cause notice for Rs.1.36 crore out of which duty of Rs.23.53 lakh had since been recovered. Reply in the remaining cases has not been received (November 1997).

The Ministry admitted (between May and December 1997) objection in seven cases. Reply in the remaining cases has not been received.

9.7 Availment of credit by transferring balance from set off register to Modvat account

Under the provisions of rule 57H(3), a manufacturer can, with the approval of the Assistant Commissioner, transfer credit of duty paid in his account in RG 23A on input materials or component parts received by him and lying unutilised immediately before filing the declaration under rule 57G for availing Modvat credit on inputs, if he had been availing of the special procedure under rule 56A and the unutilised credit was lying in his account maintained in RG 23. The Tribunal, in the case of Sirpur Paper Mills {1996 (82) ELT 212 (T)} also decided (4 August 1995) that the transfer of credit of duty on the input materials and lying unutilised is permitted only if the credits were entered and were available in the assessee's account in RG 23. The Tribunal also held that granting of

permission to transfer credit from set off register to RG 23A (Modvat credit account) would be against the provisions of the Act/Rules.

A manufacturer of cigarettes, in Hyderabad Commissionerate, was following set off procedure for making adjustment of the duty paid on tobacco used in the manufacture of cigarettes by virtue of a notification dated 24 June 1986. On extension of the Modvat credit facility to cigarettes from 16 March 1995, the assessee was allowed to take Modvat credit equivalent to the amount lying unadjusted in the set off register. Since the assessee was not following special procedure of rule 56A and credit was not lying in RG 23, permission granted to take Modvat credit was not in order. This resulted in incorrect availment of credit of Rs.1.41 crore.

On being pointed out (October 1996), the department stated (January 1997) that the transfer of credit was allowed under the orders of Commissioner (Appeals).

Reply of the department is not tenable in view of specific provisions of rule 57H(3) and the decision of jurisdictional CEGAT. Further, the department also could not produce the said orders of Commissioner (Appeals) allowing such a transfer of credit.

Reply of the Ministry has not been received (November 1997).

9.8 Availment of credit without declaration

As per rule 57 G of the Rules, a manufacturer intending to take credit of the duty paid on inputs under rule 57A shall file a declaration with the proper officer of the Central Excise department, indicating the description of the final products manufactured in the factory and the inputs intended to be used in each of the final product and obtain a dated acknowledgement of the said declaration. The Board in it's letter dated 9 February 1988, clarified that such declaration should indicate the description and sub-heading of both the inputs and final product. Further, the tribunal in the case of M/s. P.G. Conductors {1996 (81) ELT 336} decided that the requirement of rule 57G relating to declaration "is not just a technical formality or a procedural requirement but the use of the words in the rule clearly brings out that the Modvat credit can be taken only after filing

the declaration and obtaining acknowledgement, thereof". Thus, the requirement of the rule is substantive.

Eleven assessees, (Bhubaneswar (1), Chandigarh (4), Cochin (1), Hyderabad (1) Meerut (2), Mumbai III (1) and Surat (1) Commissionerates), engaged in the manufacture of various excisable products, were allowed to avail and utilise Modvat credit of duty paid on inputs, notwithstanding the fact that the declarations indicating the description of inputs or the outputs were not filed by the assessees. The utilisation of credit of Rs.1.41 crore between April 1988 and September 1996 was, therefore, incorrect.

On being pointed out (between August 1991 and January 1997), the department admitted objection in one case and intimated (between May 1996 and February 1997) issue of show cause notices for Rs.86.46 lakh in four other cases. Department in five cases and the Ministry in a case, contended (May 1997) that non-filing of declaration was only a procedural irregularity, technical in nature. It was further contended that the Tribunal in the case of Chamundi Steel Re-rolling Mills {1996 (81) ELT 568} has held that Modvat credit should not be denied merely on grounds of non-filing of declaration.

Reply is not tenable as it is contradictory (i) to the Tribunal's decision in the case of P.G. Conductors (cited above), (ii) to the clear provisions of rule 57G and (iii) to the clarification of the Board of February 1988. Further, in view of the anomalous situation created because of different decisions of the Tribunal on the same issue, the Board/Ministry should have clarified their stand.

Reply of the Ministry in remaining ten cases has not been received (November 1997).

9.9 Availment of credit on inputs cleared for job work

According to rule 57F(3) of the Rules, a manufacturer may remove the Modvat credit availed inputs, without payment of duty to a place outside the factory for the purpose of manufacture of intermediate products and obtain the processed goods back alongwith waste and scrap arising in the course of such operation.

Thirteen assessees, in nine Commissionerates, who had availed Modvat credit on inputs, removed these inputs to various job workers for further processing and return. The inputs on which Modvat credit of Rs.1.17 crore was availed were cleared to job workers for processing between April 1993 and September 1996 but these were however, not received back after processing. Neither did the assessee pay any duty due nor did the department demand any duty. This resulted in non-levy of duty of Rs.1.17 crore.

On being pointed out (between December 1994 and March 1997), the department admitted the objection in eight cases and reported recovery of Rs.1.10 crore. Reply in the remaining five cases had not been received (November 1997).

The Ministry admitted (between May and December 1997) the objection in four cases. Reply in remaining nine cases has not been received.

9.10 Availment of credit on inputs written off/rejected or destroyed

i) An assessee, in Bangalore Commissionerate, engaged in the manufacture of integrated line and trunk exchange was allowed to avail Modvat credit of Rs.66.67 lakh on inputs which were written off in the annual accounts of the company for the year 1994-95, due to obsolescence. The corresponding credit of Rs.66.67 lakh was utilised for payment of duty on other final products where such inputs were not used. Similarly, two assessees, in Nagpur and Bhubaneswar Commissionerates, were allowed to avail credit of Rs.13.10 lakh on rejected purified terephthalic acid and high density polyethylene bags which were not used in the final products. Availment of credit without utilisation of inputs, resulted in an incorrect availment of Modvat credit of Rs.79.17 lakh.

On being pointed out (December 1995), the department contended in two cases that the reversal of Modvat credit arises only at the time of removal of inputs from the factory. It also cited the decision of CEGAT in the case of M/s. Bharath Berg Limited {1995 (80) ELT 312} in support of its contention.

The reply is not relevant as in the case cited by the department, the tribunal had decided the question of treating the C.R. coils as input or as waste if it becomes defective

after undergoing some manufacturing process. Further, the credit is admissible only if input goods are used in or in relation to the manufacture of final products, the inputs rejected before under going manufacturing process could not be treated as used in the manufacture of the final products.

Reply of the Ministry has not been received (November 1997).

ii) An assessee, in Delhi Commissionerate, engaged in the manufacture of refrigerators was allowed to avail Modvat credit on inputs which were totally destroyed in a fire which broke out in the godown of the assessee on 3 March 1995. The credit of Rs.39.56 lakh availed on the inputs was incorrect.

On being pointed out (April 1996), the department admitted (June 1996) the objection and intimated recovery of Rs.39.56 lakh in April 1996.

The Ministry stated (July 1997) that a show cause notice for confirmation of duty paid by the assessee and for imposition of penalty has been issued.

9.11 Availment of credit on inputs cleared as such

As per rule 57F(1)(ii) of the Rules, the inputs in respect of which the credit of duty is allowed under rule 57A, may be removed from the factory for home consumption subject to obtaining dated acknowledgement from the Assistant Commissioner and on payment of appropriate duty of excise, as if such inputs have been manufactured in the factory.

i) An assessee, in Mumbai III Commissionerate, availed Modvat credit of Rs.44.05 lakh of duty paid on 6832 kilo litres of kerosene. The kerosene was later returned to the despatching refinery but duty due was not paid on kerosene. This resulted in incorrect availment of credit of Rs.44.05 lakh during November 1995 to February 1997.

This was pointed out in May 1997; reply of the Ministry/department has not been received (November 1997).

ii) Three assessees, in Chandigarh, Cochin and Mumbai III Commissionerates, availed Modvat credit on HR/CR coils, M.S. coils/strips, tyres etc. and cleared these inputs from the factory on payment of duty at the rate at which credit was availed instead of at the rate and value prevalent at the time of clearance. This resulted in short levy of duty of Rs.34.10 lakh between March 1993 and May 1996.

On being pointed out, the department reported (between June and November 1996) recovery of Rs.15.08 lakh from two assessees and stated that show cause notice was being issued to the third assessee.

The Ministry confirmed the facts in one case. Reply in the remaining two cases has not been received (November 1997).

9.12 Availment of credit on inputs not received

Four assessees, in Mumbai III and one in Allahabad Commissionerates, availed Modvat credit on the basis of quantity shown in the duty paying documents. It was noticed that the quantity actually received was less than the quantity mentioned in these documents. This resulted in incorrect availment of credit of Rs.30.22 lakh between March 1995 and December 1996 on inputs not actually received.

On being pointed out (between May 1995 and April 1997), the department accepted the objection and intimated (February and June 1997) recovery of Rs.8.50 lakh in four cases and confirmation of demand of Rs.29.98 lakh with penalty of Rs.10 lakh in the fifth case.

Reply of the Ministry has not been received (November 1997).

9.13 Non-levy of duty on waste and scrap obtained out of inputs

As per rule 57F(5)(a), any waste arising from the processing of inputs in respect of which Modvat credit has been taken may be removed on payment of duty as if such waste is manufactured in the factory.

Six assessees, in four Commissionerates, obtained waste and scrap during processing of inputs on which Modvat credit had already been availed. They cleared waste and scrap without payment of duty. Clearances of such waste without payment of duty was in contravention of rule 57F(5) and resulted in non-payment of duty of Rs.22.82 lakh during 15 January 1993 to 31 August 1996. The department also did not take any action to recover the duty due.

On being pointed out (between October 1993 and October 1996), the department intimated (between April 1996 and March 1997) that show cause notices for Rs.19.73 lakh in four cases had since been issued, out of which demand of Rs.3.73 lakh has been confirmed. In the remaining two cases, the department justified the clearances of waste without payment of duty quoting Boards circular of 19 April 1989 and CEGAT's decision in the case of Chloride Industries Limited.

The contention of the department is not tenable in view of the specific provision under rule 57F(5). Further, the decision of CEGAT was essentially based on Board's circular of 19 April 1989, which was withdrawn by the Board itself on 12 January 1993 with the clarification that the removal of waste/scrap of any kind would be covered only under rule 57 F(4), now rule 57F(5).

The Ministry admitted (September 1997) the objection in one case. Reply in the remaining cases has not been received (November 1997).

9.14 Availment of credit of customs duty

Two assessees, in Vadodara and Calcutta II Commissionerate, were allowed to avail credit of the basic customs duty paid on imported goods between February and May 1996 which was incorrect as credit of basic customs duty was not permissible under rule 57A. This resulted in incorrect availment of credit of Rs.17.71 lakh.

On being pointed out (May and June 1996), the Ministry admitted (May and June 1997) the objections and intimated recovery of Rs.17.71 lakh.

9.15 Other cases

In fourteen other cases of incorrect availment of Modvat credit, the Ministry/department, while accepting objection involving Rs.90.62 lakh, reported recovery of Rs.56.29 lakh till November 1997.

10. CLASSIFICATION OF EXCISABLE GOODS

The rates of duty leviable on excisable goods are prescribed under various headings in the Tariff. Some illustrative cases of incorrect classification of goods which resulted in short levy of duty are given in the following paragraphs:

10.1 Machinery, parts and appliances

i) Electric traction motors

Electric motors are liable to duty under heading 85.01. The Board in its Tariff Advice dated 27 March 1980 clarified that electric traction motors used in the diesel/electric locomotives are classifiable as electric motors.

An assessee, in Bolpur Commissionerate, manufactured electric traction motors and used them in the manufacture of railway locomotives, without payment of duty treating them to be exempted parts of locomotives. Since electric traction motors were not parts of these locomotives, they were correctly classifiable under heading 85.01. This resulted in short levy of duty of Rs.14.02 crore during January 1994 to June 1995.

On being pointed out (August 1995), the department admitted the objection and added (December 1996) that a show cause notice was under issue.

Further verification revealed that the classification list was approved by the department on 29 January 1997 on the lines suggested by Audit.

Reply of the Ministry has not been received (November 1997).

ii) Uninterrupted power supply system

Electrical machines and apparatus having individual functions, not included elsewhere in chapter 85, are chargeable to duty under heading 85.43 of the Tariff.

As per decision of the Tribunal in the case of J.K. Synthetics Limited {1995 (80) ELT 208 (T)}, uninterrupted power supply system (UPSS) comprising of invertors, rectifiers, output-input assembly, circuit breakers and static by-pass, etc. are classifiable under sub-heading 8543.80 of the Customs Tariff (Central Excise sub-heading 8543.00) as other electrical machines and apparatus having individual functions.

Two assessees, in Ahmedabad Commissionerate, manufactured uninterrupted power supply system, adjustable frequency invertor and electronic invertor device and classified them under heading 85.04 which covered electrical transformers, static convertors and inductors. As the products were similar to UPSS and were having individual functions, they were correctly classifiable as other 'electrical machines and apparatus' under heading 85.43. The incorrect classification resulted in short levy of duty of Rs.2.84 crore between April 1993 and March 1996.

On being pointed out (January 1995 and February 1996), the Ministry admitted (June 1997) the objection in a case. Reply in the second case has not been received (November 1997).

iii) Parts of refrigerators

As per note 1(e) of chapter 94, furniture specially designed as parts of refrigerators of heading 84.18 are not covered under chapter 94. Accordingly, table tops designed specially for refrigerators are classifiable correctly under heading 84.18 as parts of refrigerators.

An assessee, in Delhi Commissionerate, engaged in the manufacture of table tops for refrigerators classified the product as furniture under heading 94.03. As table tops were specially designed for refrigerators, they were correctly classifiable as parts of refrigerators under heading 84.18. Incorrect classification resulted in short levy of duty of Rs.23.26 lakh during 1995-96.

On being pointed out (August 1996), the department contended (September 1996) that table tops were not parts of refrigerators as they were simply placed on the top of the refrigerating units without forming any essential part of the refrigerators.

Reply of the department is not tenable in view of note 1 (e) of chapter 94.

Reply of the Ministry has not been received (November 1997).

10.2 Products of chemical and allied industries

i) Enzymes

Pharmaceutical products are classifiable under chapter 30, whereas enzymes and prepared enzymes are classifiable under heading 35.07 of the Tariff.

An assessee, in Chandigarh Commissionerate, manufactured "penicillin-G-amidase" and cleared it under heading 30.02 at 'nil' rate of duty. The manufacturing process of the product revealed that the product being a bio-catalyst, acted as an enzyme/yeast for converting the penicillin-G-salt into 6 amino penicillinic acid (6-APA). The product was, therefore, an enzyme and classifiable correctly under heading 35.07 and not under heading 30.02. Further, the same product "penicillin-G-amidase" was being classified under heading 35.07, while being imported into India, by the customs wing of the department. This resulted in short levy of duty of Rs.3.25 crore during April 1990 to March 1996.

On being pointed out in January 1993 and again in March 1997, the department admitted (January 1997) the audit objection and issued show cause cum demand notice for Rs.3.36 crore.

Reply of the Ministry has not been received (November 1997).

ii) Maximum daily face wash

Beauty or make up preparations and preparations for the care of the skin attract duty at 40 per cent ad valorem under heading 33.04.

A manufacturer, in Mumbai II Commissionerate, manufactured a product named "maximum daily face wash" and cleared it under heading 34.02 which covered 'organic surface active agents (other than soap), surface active preparations, washing preparations and cleaning preparations'. As the product in question was fit for cleaning the face as well as for taking care of the skin, it was appropriately classifiable under heading 33.04 as a 'cosmetic'. Incorrect classification of the product resulted in short levy of duty of Rs.19.91 lakh during June 1995 to March 1996.

On being pointed out (April 1996), the department while accepting the incorrect classification contended (March 1997) that the issue was already taken up by drawing sample on 29 April 1996 and issuing of a show cause cum demand notice on 15 July 1996.

Reply of the department is not tenable as audit observations were communicated to the department in April 1996 and action was taken only thereafter. Subsequent verification showed recovery of Rs.39.96 lakh for the period June 1995 to March 1997.

Reply of the Ministry has not been received (November 1997).

iii) Gulabari

Heading 33.01 of the Tariff, covers aqueous distillates and aqueous solutions of essential oils. As per note 1(c) and 1(d) of chapter 30 of the Tariff, aqueous distillates or aqueous solutions of essential oils, suitable for medicinal uses and preparations of chapter 33 even if they have therapeutic or prophylactic properties are not covered under chapter 30 as pharmaceutical products.

An assessee, in Calcutta I Commissionerate, manufactured rose water 'gulabari' and cleared it on payment of duty at a lower rate of duty classifying the product under

sub-heading 3003.30 as 'ayurvedic medicine'. The department also allowed it to be cleared as an ayurvedic medicine. It was noticed in audit that the product was only a distilled extract derived from rose petals alongwith a certain percentage of preservatives and was, therefore, classifiable under heading 33.01. Incorrect classification of the product resulted in short levy of duty of Rs.17.45 lakh during March 1994 to September 1996.

On being pointed out (November 1995 and May 1997) the department admitted (June 1997) the objection and issued show cause cum demand notices for Rs.29.57 lakh for the period August 1991 to March 1996.

Reply of the Ministry has not been received (November 1997).

10.3 Plastics and rubber

i) Plastic sheets

Heading 39.20 of the Tariff covers other plates, sheets, films, foils, and strips of plastics, non-cellular, whether lacquered or metalised or laminated.

As per note 10 to chapter 39 of the Tariff, the expression "plates, sheets, foils, films and strips in headings 39.20 and 39.21 applies only to plates, sheets, film, foil and strips and to blocks of regular geometric shape, whether or not printed or otherwise surface-worked, uncut or cut into rectangles (including squares) but not further worked (even if when so cut they become articles ready for use)". Thus, as per aforesaid note, sheets, plates blocks etc., which are not further worked but are only cut and have become articles ready for use, are to be classified under headings 39.20 or 39.21 and not as articles of plastics in residuary heading 39.26.

a) An assessee, in Aurangabad Commissionerate, manufactured plastic sheets under brand name and cleared them at nil rate of duty by classifying under sub-heading 3926.90. The product was in the form of flexible plastic hollow corrugated sheet which was not further worked but was only cut. Accordingly, it merited classification under heading

39.20 as sheet and not under heading 39.26 as other articles of plastics. Incorrect classification of the product resulted in short levy of duty of Rs.1.82 crore during April 1993 to March 1996.

On being pointed out (June 1996), the department issued show cause cum demand notice for Rs.98.51 lakh for the period December 1995 to May 1996 but contended (October 1996) that under the old tariff the product was classifiable as articles of plastic in accordance with the decision of the Tribunal (July 1986).

Reply of the department is not relevant since decision of July 1986 of the Tribunal related to old Tariff and in the new Tariff, such products have specifically been included under heading 39.20.

Reply of the Ministry has not been received (November 1997).

b) An assessee, in Calcutta I Commissionerate, manufactured sheets for use as packaging material. The declared specifications of the final product were indicative of predominance of plastics. The product was, therefore, appropriately classifiable as plastics under heading 39.20. The product was, however, incorrectly classified under heading 76.07 as an article of aluminium leading to short levy of duty of Rs.27.28 lakh for the period May 1992 to March 1993.

On being pointed out in November 1993, the objection was admitted by the Ministry (December 1994). Though the objection was accepted by the Ministry, no corrective action was taken by the department and the mistake persisted, resulting in total short levy of Rs.47.34 lakh between May 1992 and September 1994. Department's inaction to collect revenue resulted in a further loss of Rs.28.34 lakh by way of interest.

On being pointed out again (December 1994) in audit, the department stated (April 1996) that action was being taken to reclassify the product. Further development has not been intimated (November 1997).

Reply of the Ministry has not been received (November 1997).

ii) Polyethylene

High Court of Madhya Pradesh in the case of M/s. Raj Pack Well Limited {1990 (50) ELT 201} decided (November 1989) that high density polyethylene (HDPE) strips/tapes/sacks are goods made of plastics and not of synthetic textiles materials and are classifiable under chapter 39 which covers plastics and articles thereof.

An assessee, in Chandigarh Commissionerate, manufactured HDPE tapes and sacks cleared them on payment of duty at lower rate of duty classifying products under chapter 63 as textile articles. The products were made of plastics and hence were classifiable under sub-heading 3923.90 as plastic articles. This resulted in short levy of duty amounting to Rs.71.92 lakh during April 1991 to November 1992.

On being pointed out (May 1993), the department contended (March 1997) that no instructions to change the classification were received from the Board till 24 September 1992 and the said judgement was not binding on them.

Reply of the department is neither tenable nor consistent as the judgement of various Courts are indeed binding - as also accepted by the Ministry itself, in its reply to Public Accounts Committee in relation to para 3.22 of Audit report 1989-90. Further, the Board took about three years to issue instructions, thereby resulting in loss of revenue of Rs.71.92 lakh in one case alone. Total loss of revenue, if all other assessees manufacturing similar products are taken into account, would be much more.

Reply of the Ministry has not been received (November 1997).

iii) Plastic tubes and pipes

Tubes, pipes and hoses, and fitting therefor, of plastics are classifiable under heading 39.17 of the Tariff.

A manufacturer, in Delhi Commissionerate, manufactured rigid PVC pipes/tubes and cleared them at nil rate of duty under the residuary heading 39.26. As the product

was specifically classifiable under heading 39.17, the incorrect classification resulted in short levy of duty of Rs.64.30 lakh during April 1995 to January 1996.

On being pointed out (August 1996), the department admitted the objection and stated (April 1997) that the assessee had since deposited Rs.18.69 lakh and the demand for the balance amount of Rs.47.10 lakh has been confirmed.

iv) Builder's ware of plastic

Parts of cooling towers made of plastics are classifiable under heading 39.25 as builder's ware of plastics, not elsewhere specified or included in any other heading of chapter 39 of the Tariff.

An assessee, in Meerut Commissionerate, engaged in the manufacture of parts of cooling towers viz., glass fibre reinforced plastic grid, PVC channel, PVC retainer, glass fibre reinforced plastics for housings segments etc., classified the goods under heading 84.19 as parts of air conditioning machineries and the like instead of under heading 39.25. Incorrect classification of the goods resulted in short levy of duty amounting to Rs.27.59 lakh during March 1993 to July 1994 only.

On being pointed out (May 1994), the Ministry admitted (June 1997) the audit objection.

v) Conduit tubings

Conduit tubings made of plastic consisting of profiles of a duct and top cover are appropriately classifiable under heading 39.26 as other articles of plastics.

An assessee, in Coimbatore Commissionerate, manufactured 'conduit tubings' of plastics and classified them as insulator under heading 85.47 instead of correctly under heading 39.26. This resulted in short levy of Rs.15.92 lakh during April 1993 to March 1996.

On being pointed out (July 1996), the Ministry admitted (August 1997) the audit objection.

10.4 Mineral products

i) Carbon black feed stock

Heading 27.07 of the Tariff covers oils and other products of the distillation of high temperature coal tar; similar products in which the weight of the aromatic constituents exceeds that of the non-aromatic constituents. Other residues of petroleum oils or of oils obtained from bituminous materials including heavy petroleum stock are classifiable under heading 27.13.

An assessee, in Mumbai III Commissionerate, manufactured carbon black feed stock, classified the goods under sub-heading 2713.30 and cleared them on payment of duty at lower rate of 10 per cent ad valorem to a buyer. The buyer was also importing carbon black feed stock of similar aromatic contents and the imported goods were classified under heading 27.07. The incorrect classification of carbon black feed stock produced locally under heading 27.13 instead of under heading 27.07, resulted in short levy of duty of about Rs.92.81 lakh during 1994-95 and 1995-96.

Incorrect classification of the product was pointed out in February and December 1996; reply of the Ministry/department has not been received (November 1997). Subsequent verification of the record showed that the product was classified under heading 27.07 from 23 July 1996 and show cause notice for Rs.1.29 crore was under issue.

ii) Burnt lime

As per note 2 to chapter 25 of the Tariff, headings 25.01, 25.03 and 25.05 do not cover products that have been roasted, calcined or obtained by mixing.

An assessee, in Jaipur Commissionerate, manufactured 'burnt lime'(CaO) and classified the product under heading 25.05. Since burnt lime was obtained by a process

of calcination at a high temperature, it was not classifiable under chapter 25 but was classifiable under heading 28.25 as an oxide of calcium (CaO). The incorrect classification resulted in short levy of duty of Rs.54.91 lakh during April 1994 to November 1996.

On being pointed out (December 1996), the department contended (December 1996) that the purity of burnt lime in the product was 81 per cent and hence chapter note was not applicable.

The reply is not tenable as 'burnt lime' was obtained by a process of calcination and hence it was out of purview of chapter 25 in view of specific exclusion provisions. Further, CEGAT in the case of Mettur Chemical and Industrial Corporation {1994 (73) ELT 567 (T)} had also upheld the same view.

Reply of the Ministry has not been received (November 1997).

iii) Cement based chemicals

As per rule 3(b) of the Rules for the Interpretation of the Tariff, mixtures, composite goods consisting of different materials or made up of different components, which cannot be classified with reference to the specific description provided under each heading in the Tariff, shall be classified as if they consisted of the material or component which gives the product its essential character.

An assessee, in Bolpur Commissionerate, engaged in manufacturing of various kinds of construction materials (chapter 38) manufactured products namely (i) sika grout 214 (ii) anchor NSG (iii) sika refit and (iv) sika top 'B' component and classified them under heading 38.16 as refractory cement. The aforesaid products consisted of raw materials, namely cement, sand and non-shrink chemicals with cement as the principal ingredient.

The literature of the products as well as declaration by the assessee disclosed the fact that the products were cement based chemicals prepared by mechanical blending and supplied in dry powder form for use in civil construction works. Since the products were

manufactured out of cement as the principal ingredient (sub-heading 2502.90) and had the essential characteristics of mineral products (chapter 25), they were rightly classifiable under sub-heading 2502.90. Failure to classify the products correctly, resulted in short levy of duty of Rs.36.47 lakh during April 1993 to March 1997.

On being pointed out (March 1996, March 1997), the department contended (October 1996) that rule 3 (b) of the Rules, ibid, would not be applicable as the products found a specific tariff nomenclature under heading 38.16.

The reply of the department is not tenable since the heading 38.16 is applicable for the refractory cement, mortars etc., for use in furnace linings or for the manufacture of dental or jewellery moulds as per explanation under heading 38.16 of H.S.N.

Reply of the Ministry has not been received (November 1997).

10.5 Motor vehicle bodies

The Punjab and Haryana High Court in the case of Darshan Singh Pavitar Singh {1988 (34) ELT 631} held that 'motor vehicle bodies' built by independent body builders on the duty paid chassis supplied by customers are to be classified under heading 87.07, even though the goods emerging from body builder's premises is a complete motor vehicle falling under heading 87.01 to 87.05. The High court of Madhya Pradesh in the case of Rajasthan Coach Builders concurred with this decision {1992 (58) ELT 471}. In the case of Kamal Auto Industries {1996 (82) ELT 558 (T)} CEGAT also decided that 'motor vehicle bodies' built by independent body builders is rightly classifiable under heading 87.07.

An assessee, in Hyderabad Commissionerate, engaged in the building of motor vehicle body, classified the 'motor vehicle bodies' built by him under heading 87.02 and 87.04. This was incorrect since the 'bodies' built by the assessee were correctly classifiable under heading 87.07. This resulted in short levy of duty of Rs.89.06 lakh during April 1991 to December 1996.

On being pointed out (October 1994), the department stated (January 1995) that the judicial decisions were not acceptable as the products emerged into a complete motor vehicle and not body alone and hence the Ministry had filed a special leave petition in the Supreme Court (1991) against the Punjab and Haryana High court judgement.

The reply of the department is not tenable as the said High Court's Judgement, is binding on the department till such time as the Supreme Court passes an order contrary to or annulling the said order of the High Court. Further, as no show cause notice for protection of the revenue had been issued, recovery of revenue is doubtful in the event the Supreme Court confirms the judgement of the High Court.

Reply of the Ministry has not been received (November 1997).

10.6 Articles of base metals

i) Steel tubular poles

Structures and parts of structures of iron or steel are classifiable under heading 73.08 of the Tariff. The Board in its circular dated 20 July 1990 clarified that steel tubular transmission poles were classifiable under sub-heading 7308.90. But the CEGAT (special bench) New Delhi, in the case of M/s. Quality Steel Products {1993 (65) ELT 513} decided on 4 December 1992, that steel tubular poles would be classifiable under heading 73.06. It, therefore, follows that after the CEGAT judgement such goods were classifiable under heading 73.06 and not 73.08 as clarified earlier by the Board.

Five assessees, one in Bolpur and four in Calcutta II Commissionerates, were allowed to classify steel tubular poles under sub-heading 7308.90 and to clear them on payment of concessional rate of duty. As the subject goods were correctly classifiable under heading 73.06 as per CEGAT judgement cited above, the classification was incorrect and resulted in short levy of duty of Rs.21.25 lakh during 1993-94.

On being pointed out (May 1995 and February 1996), the Ministry stated (July and September 1996) that an appeal against the CEGAT judgement dated 4 December 1992 was filed in the Supreme Court.

The reply of the Ministry is not based on up-to-date facts as the Supreme Court had dismissed the appeal on 12 March 1996.

ii) Aluminium structures

Aluminium structures and parts of structures are classifiable under sub-heading 7610.90 of the Tariff.

An assessee, in Meerut Commissionerate, engaged in the manufacture of aluminium structures and parts thereof, classified the goods under heading 83.02 instead of under sub-heading 7610.90. Incorrect classification of the product resulted in short levy of duty of Rs.16.10 lakh during 1989-90 to 1994-95.

Incorrect classification was pointed out in August 1994. Subsequent verification (December 1996) showed that the department had rectified the error prospectively (with effect from 26 October 1994) but no action was taken to raise demand of the duty short levied prior to 26 October 1994.

Reply of the Ministry has not been received (November 1997).

10.7 Other cases

In seven other cases of incorrect classification, the Ministry/department, while accepting objection involving duty of Rs.71.57 lakh, reported recovery of Rs.4.09 lakh till November 1997.

11. EXEMPTIONS TO SMALL SCALE MANUFACTURERS

Duty reliefs and exemptions are allowed to small scale manufacturers of specified excisable goods under various exemption notifications issued from time to time by the Ministry of Finance. The reliefs and exemptions are subject to fulfilment and observance of conditions that are prescribed in the relevant notifications. A few illustrative cases of incorrect grant of such exemptions are mentioned below:

11.1 Goods bearing brand name of others

Under the provisions of notification dated 28 February 1993, specified goods are not eligible for exemption if they bear a brand name or trade name (registered or not) of another manufacturer who himself is not eligible for grant of exemption, under the notification, ibid. The Tribunal in the case of M/s. Super Star Welding India Limited {1994 (71) ELT 443}, held that exemption was not available on goods bearing a logo and colour scheme of another manufacturer, who himself is not eligible for such an exemption.

Three assessees, in Belgaum, Chandigarh and Hyderabad Commissionerates manufactured lathe machines, voltage stabilizers, cordless telephones etc., and cleared them by using trade or brand name or logo of other manufacturers who were themselves not eligible for exemption. Notwithstanding the fact that such goods did not qualify for exemption, the exemption was allowed. This resulted in short levy of duty of Rs.51.85 lakh between September 1991 and September 1996.

On being pointed out (between September 1993 and August 1995), the Ministry admitted the objection in two cases and intimated (March and June 1997) that show cause notice for Rs.36.72 lakh had since been issued in these two cases. Reply in the third case has not been received (November 1997).

11.2 Exemption availed by ineligible manufacturers

Exemption under notification dated 28 February 1993 shall not apply, if the aggregate value of clearances of all excisable goods for home consumption (i) by a manufacturer, from one or more factories or (ii) from any factory, by one or more manufacturers, had exceeded Rs.200 lakh, in the preceding financial year. The limit of Rs.200 lakh has been increased to Rs.300 lakh with effect from 1 April 1995. The Tribunal in the case of M/s. Gavs Laboratories (P) Limited decided {1994 (71) ELT 717} that the goods traded within India by a manufacturer for export by another party would be a clearance for home consumption only and would, therefore be included in the overall clearances for home consumption during a year to determine the eligibility of exemption under the notification, ibid.

a) Three manufacturers in Bangalore, Delhi and Hyderabad Commissionerates, were allowed to avail exemption between April 1993 and March 1995, notwithstanding the fact that the aggregate value of clearances during the relevant preceding financial years had exceeded Rs.200 lakh. This resulted in incorrect grant of exemption of Rs.19.83 lakh between April 1993 and May 1994.

On being pointed out (September 1993 and May 1996), the department admitted (September 1996 and May 1997) the objection in two cases and intimated issue of show cause notice for Rs.7.50 lakh in a case. Reply in the third case and further progress in the cases admitted has not been received (November 1997).

Reply of the Ministry has not been received (November 1997).

b) Similarly, three manufacturers, in Surat Commissionerate, were allowed to avail exemption during 1995-96 on their products though the aggregate value of clearances including clearances made to different parties in India for export during the preceding financial year 1994-95 had exceeded Rs.300 lakh. This resulted in incorrect grant of exemption of Rs.20.52 lakh.

On being pointed out (July and September 1996), the department contended (November 1996) that the Tribunal's decision had not been finally accepted. It further stated that the value of clearances during 1994-95 were less than Rs.300 lakh as the value of goods cleared for export was not includible in the aggregate value of clearances.

The reply of the department is not tenable as the goods were not exported by the manufacturers themselves but were cleared to different parties in India who were merchant exporters and proof of export was not available with the assessee. Further the action was to be taken by the department in accordance with the Tribunal's decision till it was reversed.

Reply of the Ministry has not been received (November 1997).

c) Similarly, two manufacturers, in Chennai and Surat Commissionerates, engaged in the manufacture of polyester filament yarn/diaphragm assembly, were allowed to avail exemption under the above notification, though the aggregate value of clearances for home consumption had exceeded Rs.300 lakh in the preceding financial year 1995-96. This resulted in incorrect availment of exemption of Rs.13.44 lakh during 1996-97.

On being pointed out (August and November 1996), the Ministry/department accepted (March and May 1997) the facts and intimated recovery of Rs.13.44 lakh.

11.3 Other cases

In three other cases, the Ministry/department, while accepting objections involving duty of Rs.32.68 lakh, reported recovery of Rs.26.57 lakh till November 1997.

12. MONEY CREDIT SCHEME

The scheme extends monetary credit on certain inputs at specified rates for use towards payment of duty on final products under the terms and conditions prescribed in rules 57K to 57P of the Rules.

Some of the illustrative cases of incorrect availment of money credit noticed in test audit are mentioned in the following paragraphs:

12.1 Incorrect availment of money credit

As per notification dated 11 October 1989 as amended, credit of money at the specified rates can be taken in respect of inputs, namely vegetable oil/fat of the description specified in the notification. Further, as per condition (i) of notification ibid, money credit shall be taken on the date on which the oil has been hydrogenated, blended or emulsified.

Two assessees, availed money credit either before the date of hydrogenation or on inputs not specified in the notification. The availment of money credit of Rs.92.01 lakh between March 1988 and March 1996, in contravention of the terms of the notification was, therefore, incorrect.

On being pointed out (between September 1993 and July 1996), the Ministry intimated (September 1996) that a demand of Rs.89.95 lakh had since been confirmed and penalty of Rs.10000 imposed in one case. Reply of the Ministry in the other case has not been received (November 1997).

12.2 Credit availed without production of requisite certificates

According to condition (iv) of the notification dated 11 October 1989, where credit has been taken in respect of any solvent extracted variety of the oils specified in the notification, the manufacturer shall, within five months from the date of taking credit or such extended period as the Assistant Commissioner may allow, produce a certificate

from an officer not below the rank of Deputy Director in the Directorate of Vanaspati, Vegetable Oils and Fats in the Ministry of Food and Civil Supplies, to the effect that the said oil had been manufactured by the solvent extraction method.

Five assessees, engaged in the manufacture of vegetable products, availed money credit amounting to Rs.10.31 lakh between April 1994 and January 1996 on 160 tonne of 'solvent extracted mustard oil' and 158 tonne of 'solvent extracted sunflower oil'. However, the requisite certificates were neither produced within the prescribed time limit of five months nor was the period extended by the competent authority. In the absence of the requisite certificates, the availment of credit amounting to Rs.10.31 lakh was improper.

On being pointed out (between November 1995 and December 1996), the department intimated (between March 1996 and January 1997) recovery of Rs.7.71 lakh from four assessees and issue of show cause notice for Rs.3.50 lakh to fifth assessee.

The Ministry admitted objection in a case. Reply of the Ministry in the remaining cases has not been received (November 1997).

13. CESS NOT LEVIED/DEMANDED

Cesses are levied and collected in the same manner as excise duty under the provisions of various Acts of the Parliament.

Some of the cases in which cess was not levied or demanded are mentioned below:

13.1 Non-levy of cess

Cess is leviable on every article of jute specified in the schedule to the Jute Manufactures Cess Act, 1983. Rule 3 of Jute Manufactures Cess Rules, 1984, lays down that consumption of jute manufactures would attract cess at specified rates, irrespective of the fact of the removal of finished jute manufactures for export or for consumption within the country. The Supreme Court in the case of M/s. Barnagore Jute Factory Company {1992 (57) ELT 3(SC)} held that cess was leviable even when jute yarn was consumed captively. Jute yarn captively consumed for further manufacture of jute products are, therefore, liable to cess.

i) Five jute mills, in three Commissionerates, consumed jute yarn/slivers within the factory for manufacture of jute products without payment of cess amounting to Rs.67.10 lakh between April 1993 and March 1996. The department also did not demand the applicable cess.

On being pointed out (between February 1995 and March 1997), the Ministry of Textiles stated (July 1997) that jute slivers were not specifically covered in the schedule and that cess was leviable on finished jute manufactures. It was further stated that an exemption notification has been issued on 8 November 1996 with prospective effect.

The reply is not tenable as the words "any other article of jute manufacture" have been used in the schedule which covers not only jute slivers but every article of jute manufactures. Further, cess on jute slivers was paid when it was cleared for export. Therefore, cess was leviable on every article of jute manufactures and the matter requires regularisation for earlier period also.

ii) CEGAT in the case of M/s. Consolidated Builders and Developers (P) Limited {1997 (91) ELT 582} held that 'hessian bags' and 'sacking bags' manufactured out of jute hessian and jute fabrics removed for sale within the country, would be again leviable to cess under section 3 of Jute Manufactures Cess Act, 1983 read with Jute Manufactures Cess Rules, 1984.

A jute mill manufactured jute fabrics and cleared it on payment of duty and cess to different laminators for lamination of jute fabrics and then making bags. The bags so manufactured were directly sent to the customers as per manufacturer's instructions. However, cess at laminated jute bags stage was not paid though ought to have been paid as per above the mentioned Act/Rules, read with the CEGAT's judgement. This resulted in non-levy of cess of Rs.5.95 lakh during 1 April 1995 to 7 January 1997.

On being pointed out (March 1997), the department admitted the non-levy of cess but contended (June 1997) that cess was payable by the job worker since the job worker was the real manufacturer of laminated jute bags.

The department's contention is not tenable as the job worker was not the real manufacturer as fabrics and other materials were supplied free of cost and he was paid job charges only. Further, the laminated bags so manufactured were marketed by the raw material supplier and not the job worker. Hence, cess was to be paid by the assessee.

Reply of the Ministry of Textiles has not been received (November 1997).

iii) As per Ministry of Industry's, notifications dated 22 March 1990 and dated 26 May 1994, cess is leviable at the rate of 1/8 per cent ad valorem on motor cars, buses, trucks, jeep type vehicles, vans and all other automobiles. Chassis fitted with the engines and building a body on the chassis are identifiable as separate excisable products under the Tariff and are dutiable, accordingly.

Three assessees, engaged in the fabrication of bus bodies on duty paid chassis, cleared the body mounted buses on payment of appropriate excise duty but cess leviable

thereon was not paid. This resulted in the non-levy of cess amounting to Rs.8.38 lakh during April 1991 to March 1997.

On being pointed out (May 1994), the Ministry of Finance stated (June 1996) that the matter was under examination. Further progress has not been intimated (November 1997).

14. OTHER IRREGULARITIES

14.1 Abnormal delay in finalisation of provisional assessment cases - unintended financial accommodation

According to rule 9B of the Rules, the excisable goods can be assessed to duty provisionally, in cases where an assessee is unable to furnish any document necessary for the assessment of duty of any excisable goods or goods are required to be subjected to chemical test or when the proper officer deems it necessary to make further enquiry for assessment of duty. No time limit for the final assessment has been prescribed in the Rules. However, as per instructions of the Board in March 1976, cases of provisional assessment should be finalised normally within a period of three months and in any case not later than six months. Further, in normal situations interest is payable only after 3 months after the duty has been determined. That being so, any delay in finalising the provisional assessments invariably lead to loss accruing to Government by way of interest and financial accommodation to the assessee. Further, the Supreme Court, in the case of M/s. Bombay Tyre International (1983) and in the case of M/s. MRF Limited (1995) had specifically clarified as to which post manufacturing expenses (PMEs), would qualify for being allowed as deductions from the assessable value for the purpose of levying excise duty. The judgements of the Supreme Court being law of the land, all assessments/adjudications should have been finalised, accordingly.

In the absence of provisions prescribing time limit and interest in the Rules, the provisional assessments were kept pending by the department for abnormally long periods. A test check of only four cases relating to 'PMEs' in four Commissionerates, disclosed that the cases were kept pending by the department for periods ranging from thirteen to twenty three years. The differential amount of duty involved in three of these cases (in the fourth case, even the amount of differential duty had not been quantified since the last 14 years) was Rs.44.18 crore. The non-finalisation of these cases led to a loss of revenue

amounting to Rs.191.22 crore upto March 1997 by way of interest, besides blockage of revenue of Rs.44.18 crore and resultant financial accommodation to the assessees.

To avoid undue financial accommodation to the assessees due to delayed finalisation of 'provisional assessment cases', there is, therefore, an urgent need to incorporate suitable provisions in the Act/Rules, to (i) provide for a reasonable time limit for finalisation of the provisional assessment cases and (ii) make interest payable from the relevant dates of clearances of goods.

14.2 Dant manjan lal - Board's instructions to the detriment of revenue

Tooth powder is liable to duty under heading 33.06 of the Tariff.

An assessee, having two units in Calcutta II and Patna Commissionerates, was engaged in the manufacture of tooth powder in the name 'dant manjan lal'. The product was cleared at nil rate of duty classifying it under chapter 30 as 'ayurvedic medicine'. The incorrect classification leading to short levy of Rs.1.86 lakh from 2 June to 9 August 1988 in one unit and non-maintenance of production records by second unit was pointed out in audit in September 1988 and March 1990. The Ministry replied (November 1989) that the matter was under examination. The department also served seven show cause cum demand notices for Rs.31.26 lakh for the period September 1988 to May 1991.

In subsequent audit of these units, it was observed that the demand notices earlier issued by the department for the period September 1988 to May 1991 were dropped on 16 September 1992 and no demand notices were issued thereafter for similar short levy of Rs.1.50 crore for the period June 1991 to August 1996.

On being again pointed out (October 1996), the department contended that the earlier demands were withdrawn and no further demands were raised because the Board had clarified on 25 September 1991 that 'dant manjan lal' was an ayurvedic medicine and this clarification was still in force.

Reply of the department is not tenable as the issue of classification of dant manjan lal manufactured by the same assessee was already decided on 10 July 1990 by the Tribunal in favour of revenue and being aggrieved with this decision, the assessee had filed an appeal before the Supreme Court which was under consideration at that time. The above case was ultimately decided in March 1995 by the Supreme Court upholding the Tribunal's decision classifying the product under chapter 33 as "tooth powder". The issue of circular by the Board on 25 September 1991 to the detriment of revenue and notwithstanding CEGAT's judgement and even when the case was pending decision with Supreme Court, was improper and resulted in loss of revenue amounting to Rs.1.83 crore.

Reply of the Ministry has not been received (November 1997).

14.3 Delay in remitting of duty collected

Under rules 9 and 49 of the Rules, the duty becomes payable at the time of clearance of excisable goods. The Central Excise Act, provides for charging interest in cases where there is delay in payment of duty beyond three months of duty having been determined by the Central Excise Officer. There are, however, no provisions in the Act or Rules for charging interest where duty is determined by the assessee and delay in depositing duty occurs.

Two assessees, in Goa and Mumbai III Commissionerates, were clearing their products on payment of duty lower than what was leviable thereon. However, they were collecting full duty from the customers. The excess amount of Rs.17.47 crore so collected from the buyers between April 1994 and December 1996, was remitted to Government account after delay ranging from 1 to 11 months. Thus, there was a loss of interest of Rs.54.00 lakh to the Government, in the absence of provisions for charging interest in such cases.

The above points were reported to the Ministry (July 1997); reply has not been received (November 1997).

14.4 Contradictory clarification of the Board

Note 5 of chapter 30 of the Tariff dealing with 'pharmaceutical products' stipulates that in respect of goods covered under heading 30.03, conversion of powder into tablets or capsules, labelling or relabelling of containers intended for consumers and repacking from bulk packs to retail packs or the adoption of any other treatment to render the product marketable to the consumer, shall amount to 'manufacture'.

An assessee, in Mumbai I Commissionerate, engaged in the manufacture of pharmaceutical products of chapter 30 had imported finished medicines namely 'actilyse' and 'magnevists' from their principals in Germany. To make the product marketable, stickers were pasted on the cartons of imported medicines indicating the import licence number, name of the company, marketed by, product ingredients, warning and maximum retail price as required under Drug and Cosmetic Act, 1940. Therefore, in terms of the above said chapter note labelling the imported medicines to make it marketable, amounted to 'manufacture' and duty was, accordingly payable on such goods. During the year 1995-96, the assessee had cleared the imported medicines after labelling but without payment of duty, which was incorrect.

On being pointed out (March 1996), the department stated (March 1997) that the assessee had paid duty amounting to Rs.35.64 lakh from November 1995 to July 1996. However, no duty was paid by the assessee for the further period because of the issue of Board's circular dated 14 May 1996 clarifying that the process of pasting of stickers on imported medicines might not be covered by note 5 of chapter 30.

The reply of the department is not tenable as the clarification of the Board, being an executive instruction cannot override the specific provisions of the legislation contained in note 5 of chapter 30 of the Tariff.

Reply of the Ministry has not been received (November 1997).

14.5 Miscellaneous

Forty eight other objections involving duty of Rs.1.48 crore were also pointed out. The department accepted all these objections and reported recovery of an amount of Rs.1.29 crore in forty two cases till November 1997.

Vikram Chandra

New Delhi
The 08 MAY 1998

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Countersigned

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The 08 MAY 1998

(V.K. SHUNGLU)
Comptroller and Auditor General of India