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Quantum of credit on cotton yarn lying in stock – How to calculate?

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The decision to introduce the excise regime on textile sector has opened a pandora's box and a lot more issues are yet to be clarified by the authorities. In this article, we wish to dwell upon one among such issues.

Consequent to the unveiling of full fledged excise regime for the textile sector, several instructions / notifications have been issued by the Board and it is very difficult for a common man to follow them up and keep him updated. Hardly a day passes, without an official word being said on the subject.

One time Cenvat Credit is allowed in respect of the inputs lying in stock, contained in work in progress and in finished goods, for all those who are liable for payment of duty. This provision is widely known as Transitional Provision under the Cenvat Credit Rules. Cotton Yarn, being an important input for the textile sector, the one time credit is also allowed for such cotton yarn, lying in stock.

It may be observed that cotton yarn attracts BED as well as AED (T&TA). As per the Cenvat Rules, the credit of AED (T&TA) can be used only for payment of AED (T&TA), if applicable on the final products. As most of the products manufactured out of such cotton yarn, viz., unprocessed woven fabric of cotton, processed woven fabric of cotton and garments, do not attract AED (T&TA), the AED (T&TA) paid on yarn, cannot be availed as credit by the manufacturers of such goods, in the normal course.

As per the transitional provisions, if the documents indicating payment of duty of excise is available for the yarn lying in stock, the manufacturer can avail actual credit, based on the documents. This is provided for in Rule 9 A (1) of Cenvat Credit Rules, 2002, as enacted vide Notification 25/2003 NT Dated 25.3.2003. If documents evidencing payment of duty are not available, credit has to be availed, as per the procedure prescribed vide Notification 35/2003 NT Dated 10.04.2003, as amended by Notification 47/2003 NT Dated 17.05.2003. As per these Notifications, the quantum of credit that can be taken in respect of yarn shall be calculated as below:

Deemed value multiplied by the rate of duty on such yarn.

The term "deemed value" means
$$\frac{\text{Declared Value} \times 95}{100 + \text{Rate of duty}}$$

Rate of duty is explained in the Notification as, the rate of duty leviable under the Central Excise Tariff Act, 1985, the Additional Duties of Excise (Goods of Special Importance) Act, 1957 and Additional Duties of Excise (Textile and Textile Articles) Act, 1978, as the case may be, read with any notification, as on the 1st day of April 2003.

It is not clear from the Notifications, as to whether the AED (T&TA) paid on cotton yarn, shall also be considered in the "Rate of duty", envisaged in the above said formula, despite the fact that the said AED(T&TA) cannot be used by the manufacturer. In view of the omnibus Explanation of the term "Rate of duty" in the notification, without any qualification, one view would be that the rate AED (T&TA) can also be taken into consideration in the formula. Another view would be, since the use of AED (T&TA) is restricted only against the payment of AED (T&TA) on the final products, the rate of AED (T&TA) cannot be taken into account, in applying the above formula. This view can be countered by saying that the one time credit envisaged in the Notification is mere Cenvat credit and its segregation into various components of duty, is not envisaged in the Notification. This counter view can also be countered (counter squared?) by saying that if credit is taken based on the documents, the AED (T&TA) would not

have been availed. And so the maze! The implications of the above points and counter points can be better appreciated with the help of a practical example.

Let us assume that a particular quantity of cotton yarn is purchased for Rs.100, on payment of Rs.8 as BED (8 %) and Rs.1.20 as AED (T&TA) (15 % on BED) and the same is lying in stock. The invoice for the same is raised as below:

Yarn Value	:	Rs. 100.00
BED	:	Rs. 8.00
AED (T&TA)	:	Rs. 1.20
Total	:	Rs. 109.20
Sales Tax 4 %	:	Rs. 4.37
Freight	:	Rs. 1.00
Total Value	:	Rs. 114.57

Situation 1 : If purchase document for the same is available, the credit that can be availed in respect of such cotton yarn would be the BED portion i.e. Rs. 8.00. (Restricted to BED portion, as AED (T&TA) portion could not be utilized by the manufacturer. **Rs.8.00**

Situation 2 : If purchase document for the same is not available, recourse has to be made to Notification 35/2003. Here, if it is assumed that the rate of duty envisaged in the Notification includes the AED (T&TA) rate also, the quantum of credit available would be,

$$\begin{aligned}
 &\text{Declared Value Rs. 114.57} \\
 &114.57 \times 95 \\
 &\text{-----} \times 9.2 \% \\
 &100 + 9.20 \\
 &= \mathbf{Rs. 9.17}
 \end{aligned}$$

Situation 3 : If it is argued that since the AED (T&TA) credit could not be used by the manufacturer, the rate of duty would mean only the BED Rate, the quantum of credit available would be

$$\begin{aligned}
 &114.57 \times 95 \\
 &\text{-----} \times 8.0 \% \\
 &100 + 8 \\
 &= \mathbf{Rs. 8.06}
 \end{aligned}$$

There is only a marginal difference in the credit entitlement between situation 1 and situation 3. But situation 2 has far reaching implications. As recourse to this situation is not free from doubt, it would be better if more light is thrown on this issue. Readers are also requested to contribute their views. The authors of this article can be contact at asksa@rediffmail.com.

