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RULE SIX IN A FIX

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In a recent and reasoned judgment, in the case of M/s International Auto limited Vs CCE, Bihar {2005 (183) ELT 239 (SC)}, the Hon'ble Supreme Court has redefined and given a new dimension to the Excise Valuation. To appreciate better, let us first cruise through the facts of the case:

The appellant was a job worker for TELCO. TELCO had supplied some Modvat credit availed inputs to the appellant. The same were used by the appellant, along with their own inputs, to manufacture floor plate assemblies for TELCO. TELCO used such floor plate assemblies, in their further manufacture of excavators, which were subjected to duty of excise. The appellant did not avail any exemption in respect of the job work activity and were paying duty on the floor plate assemblies manufactured and cleared by them. While doing so, they paid duty only on the value of the materials used by them plus their job work charges. In other words, they did not include the value of the inputs supplied to them free of cost, by TELCO. The department disputed the valuation and alleged that the value of the inputs supplied free of cost by TELCO has to be included in the assessable value for payment of

Excise duty. The dispute finally reached the Hon'ble Apex Court.

While delivering the landmark decision, the Hon'ble Apex Court has observed that,

> *"The scheme of Modvat permits the person who clears the ultimate final product to take the benefit of the Modvat scheme at the time of clearance of such final product. The manufacturer of the final product, in this case TELCO, would therefore, be entitled not only to adjust the credit on the inputs supplied by it to the intermediate purchaser such as the appellant but also to the credit for the duty paid by the intermediate purchaser on its products".*

Accordingly, it has been laid down by the Hon'ble Apex Court that, the appellant need not include the value of inputs, supplied to them free of cost by TELCO, in the assessable value of the floor plate assemblies manufactured and cleared back by them to TELCO. While holding so, the Hon'ble Apex Court has also observed that its previous decision in the case of Burn Standard Company Limited {1992 (60) ELT 671} is not applicable, in as much as, in that case neither the Modvat scheme nor the provisions of

Rule 57 (F) (2) (b) were concerned and also in view of the fact that, the issue involved in that case is that of the valuation of the final product, whereas in the present International Auto case, it is one of an intermediate product, which would go into the final product.

Now let us analyse the possible effects of this far-reaching decision.

Normally, any inputs given free of cost by the customers (popularly known as FOC items), to the manufacturer for use in the manufacture of excisable goods, are treated as "additional consideration" for the purpose of valuation of excisable goods. The money value of such FOC items is added to the assessable value of the excisable goods for the purpose of payment of Excise duty. During the relevant period, pertaining to the International Auto case (1993), Rule 5 of the then Central Excise Valuation Rules, 1975 was the one, which dealt with such additional considerations. It read as,

> "Where the excisable goods are sold in the circumstances specified in clause (a) of sub-section (1) of section 4 of the Act except that the price is not the sole consideration, the value of such goods shall be based on the aggregate of such price and the amount of the money value of any additional consideration flowing directly or indirectly from the buyer to the assessee".

At present, the concept of "additional consideration" finds place in Rule 6 of the Central Excise Valuation Rules, 2000, which reads as:

> Where the excisable goods are sold in the circumstances specified in clause (a) of sub section (1) of section 4 of the Act except the circumstance where the price is not the sole consideration for sale, the value of such goods shall be deemed to be the aggregate of such transaction value and the amount of money value of any additional consideration flowing directly or indirectly from the buyer to the assessee.
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> *Explanation.* - For removal of doubts, it is hereby clarified that the value, apportioned as appropriate, of the following goods and services, whether supplied directly or indirectly by the buyer free of charge or at reduced cost for use in connection with the production and sale of such goods, to the extent that such value has not been included in the price actually paid or payable, shall be treated to be the amount of money value of additional consideration flowing directly or indirectly from the buyer to the assessee in relation to sale of the goods being valued and aggregated accordingly, namely : - value (i) of materials, components, parts and similar items relatable to such goods; value (ii) of tools, dies, moulds, drawings, blue prints, technical maps and charts and similar items used in the production of such goods; value (iii) of material consumed, including packaging materials, in the production of such goods;
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> (iv) value of engineering, development, art work, design work and plans and sketches undertaken elsewhere than in the factory of production and necessary for the production of such goods.

From the above, it may be observed that the basic principle behind the concept of "additional consideration" has been the same, both under the erstwhile Rule 5 and under the present Rule 6, but for the insertion of an Explanation to Rule 6, which is primarily clarificatory in nature.

Though the provisions of the above said Rule 5 have not been explicitly referred to, in the decision of the Hon'ble Apex Court (supra), the demands would have been confirmed at lower levels, only based on the said Rule 5, as it was the only relevant statutory provision, to govern the "additional considerations". As such, the present decision of the Hon'ble Apex Court has to be seen in the context of the present Rule 6 of the Central Excise Valuation Rules, 2000.

Taking cue from the ratio laid down by the Hon'ble Apex Court in the case (supra), it may be observed that, the above said Rule 6 would almost become an otiose in the statute book, for the reasons stated below.

In most of the cases, where the principal manufacturer supply inputs / components / tools / capital goods / drawings, etc, such principal manufacturer would have already availed Cenvat Credit on the same and such goods would have been removed to their job workers, either under Rule 4 (5) (a) or 4 (5) (b) of the Cenvat Credit Rules,
2004, which are *in pari materia* to Rule 57 (F) (2) (b) of the then Central Excise Rules, 1944. No doubt, in all such cases, the value of such goods supplied to the job workers would form part of the value of the final products manufactured and cleared by the principal manufacturer, on which appropriate duty of excise is paid. As such, going by the present ruling, in all such cases, the job workers who are manufacturing certain intermediate products for the principal manufacturers need not include the value of such FOC items supplied by their principal manufacturers, for the purpose of payment of duty of such intermediate products.

Now the moot question would be as to the relevance of Rule 6 of the Central Excise Rules, 2000. Viewed in the backdrop of the said judgement, it could be concluded that, Rule 6 would come into play, only in the following limited circumstances:

- Where the cost of the inputs supplied free of cost by the principal manufacturer (FOC items) are not included in the final product manufactured and cleared by the principal manufacturer. (Eg.

If the intermediate products are in the nature of accessories of final products, cleared along with the final products, the value of which is not subjected to duty).

- Where the goods supplied by the job worker are not in the nature of intermediate products but are in the nature of final products. To amplify it further, if the goods supplied by the job worker are not used in the further manufacture of excisable goods at the hands of the principal but are being sold as such (trading).

- Where the goods manufactured by the principal manufacturer, are not subjected to duty of excise.

In the above cases, the principal manufacturer would not have availed the benefit of the Cenvat Credit scheme on the final products cleared by them and hence cannot enjoy the benefit of this decision (supra). In all such cases, Rule 6 shall come into play at the hands of the job worker, whereby, the money value of such FOC items would be required to be included to the assessable value of the excisable goods manufactured and cleared by such job workers.

Before parting…

The Hon'ble Apex Court has delivered the said decision based on the eligibility of the Modvat credit scheme (now Cenvat credit) to the principal manufacturer. What would be the case, if the FOC items are in the nature of ineligible inputs (fuel) or ineligible capital goods (unspecified chapters) under the Cenvat credit scheme? Would the ratio hold good for such cases too, if the cost of such inputs or capital goods is included in the final products manufactured and cleared on payment of appropriate duty, by the principal manufacturer? In other words, whether the crux of Apex court decision lies on Cenvat provisions or on the fact that the value of such items, are included in the final product valuation?