BEFORE THE MADURAI BENCH OF MADRAS HIGH COURT

Reserved on: 04.07.23

Pronounced on: 06.07.2023

CORAM:

THE HONOURABLE **DR.JUSTICE ANITA SUMANTH**
AND
THE HONOURABLE **MR.JUSTICE R.VIJAYAKUMAR**

C.M.A.(MD)No.810 of 2015

M/s.GGN Spinning Mills (P) Ltd.,
Represented by its Director,
G.Balamurugan. ...Appellant

/Vs./

1.The Customs Excise and Service Tax Appellate Tribunal,
South Zoanl Bench,
26-Haddows Road,
Chennai – 600 006.

2.The Commissioner of Central Excise,
Bibikulam,
Madurai – 625 002. ...Respondents

PRAYER:- Appeal - filed under Section 35G of the Central Excise Act, 1944, to set aside the impugned Final Order No.41049/2014 dated 19.12.2014 (duly signed on 09.04.2015) in Appeal No.E/739/2004 passed by the learned first respondent Tribunal.

For Appellant : Mr.M.Kumar
for Mr.S.Reganathan

For Respondents : Mr.N.Dilipkumar

JUDGMENT

(Judgment of the Court was delivered by **DR.ANITA SUMANTH, J.)**

The appellant has challenged an order of the Customs, Excise and Service Tax Appellate Tribunal ('Tribunal / CESTAT' in short) dated 19.12.2014. The facts giving rise to the present appeal are as follows:

2. The appellant is engaged in the manufacture of exercisable cotton yarn falling under the Central Excise Tariff Act, 1985 (in short 'Tariff Act'). It claims MODVAT ie., Modified Value Added Tax, and has been availing credit of duty paid on inputs and capital goods used in the manufacture of dutiable and exercisable goods. The appellant has two units, A & B, and had imported machineries during the period September 1997 to April 1999. In 2022, those machineries had been transferred from A to the B Unit.

3. On 16.07.2003, a show cause notice came to be issued alleging suppression of value of the capital goods and evasion of Central Excise Duty thereupon. There was an inspection of the factory premises on 26.02.2003 when the officials noted that in arriving at the value of capital goods for the purpose of payment of excise duty, the depreciation computed under the Written Down Value method (WDV method), has been adopted, at 25%, in line with the provision under the Income Tax Act, 1961.

4. The officials were of the view that the straight line method ought to have been adopted as prescribed by the Central Board and Excise and Customs (in short 'CBEC') under Circular No.643/34/2002–CX dated 01.07.2002 (in short ‘2002 Circular’) read with Board's Letter No.495/16/93–CUS IV, dated 26.05.1993 (in short ‘1993 Board Letter’). This is the narrow controversy before this Court.

5. The book value of the machineries transferred from Unit A to B had been adopted for the purpose of reversal of CENVAT Credit. The officials noted that the original assessable value of the capital goods

was a sum of Rs.1,67,20,299/- and the credit availed thereupon was a sum of Rs.20,60,055/-. The value adopted at the time of transfer was Rs. 61,52,111/- claiming depreciation on WDV method, and the removal was on payment of duty of Rs.9,84,338/-. In doing so the Appellant relied upon Rule 4(4) of the Cenvat Credit Rules 2002 (in short 'CCR 2002').

6. Per contra, the scale of depreciation to be adopted per the Department, that applied the stipulation under the 1993 Board Letter, was as follows:

> *"(i) for every quarter during the 1st year – 4%*
> *(ii) for every quarter during the 2nd year – 3%*
> *(iii) for every quarter during the 3rd year – 2.50%*
> *(iv) for every quarter during the 4th year – 2%*

7. Adopting the above method, assessable value of goods removed was a sum of Rs.1,04,64,531/- and the duty thereupon, Rs. 16,74,325/-. The differential duty arrived at was a sum of Rs.6,89,987/-. The show cause proposed a demand of the aforesaid amount towards differential duty with penalty and interest at appropriate rates.

8. The appellant responded on 17.09.2003 and the main argument was that the 1993 Board Letter was inapplicable to the present transaction as those had been issued in the context of second-hand motor vehicles and not machineries. That apart, the Letter would not prevail over Rule 4(4) of the CCR 2002, that specifically refers to depreciation under the Income Tax Act, 1961.

9. An order in original came to be passed on 28.11.2003 confirming the proposals under the show cause notice, as against which, an appeal was filed. The appellant was successful in first appeal. The Commissioner accepted their submissions that the appropriate method of computing depreciation would be as prescribed under the Income Tax Act as the goods transferred constituted capital goods and that, in any event, the exercise was revenue neutral.

10. As against the order of the first appellate authority, the department filed an appeal which has come to be allowed on 18.01.2011. The CESTAT has proceeded on the premise that a consistent and uniform methodology was being followed in cases similar to the present matter,

by adopting the straight line method of reckoning depreciation, and there is no reason why there should be any deviation in this matter.

11. In conclusion, while upholding the choice of straight line methodology, the CESTAT found that the computation of depreciation in the show cause notice was not proper and remanded the matter for recomputation of differential duty.

12. Heard the detailed submissions of Mr.M.Kumar, learned counsel for the appellant and Mr.N.Dilipkumar, learned Panel counsel for the respondents. The following substantial questions of law have been raised:

> "*1) Whether the First Respondent correctly applied the law, for availing the depreciation Under Section 32 of the Income Tax Act incorporated in Rule 4(4) of Cenvat Credit Rules read with Rule 3(4) of Cenvat Credit Rules, in respect of removal of used capital goods as such, during the year 2002-2003 ?*
>
> *2) Whether the First Respondent erred in directing to apply straight line method of depreciation effective from 13-11-2007 read with amended Rule from 27-2-2010 by Notification No.6/2010-CE(N.T) which was not prescribed during the period of removal of such capital goods (ie.,) Financial year 2002-03 ?*
>
> *3) Whether the First Respondent's order is retrograde in nature while rejecting the application of*

Section 32 of the Income Tax Act, 1961, for depreciation used capital goods?

4) Whether the First Respondent Tribunal violated the principles of natural justice in placing the Circulars No.643/34/2002 dated 1-7-2002 read with Circular No.495/16/1993-Cus. dated 26-5-1993 without applying Section 32 of the Income Tax Act, 1961 ?

5) Whether the impugned order passed by the learned First Respondent Tribunal is proper and legal?"

13. The reversal of credit at the time of transfer of goods has been provided for in the Rules applicable from time to time. During the period 01.03.1997 to 01.04.2000, Rule 57Q and 57S of the Central Excise Rules stipulated the manner of utilisation of capital goods and the credit allowed in respect of duly paid thereon.

14. Section 57S reads as follows, and sub-Rule 2(b) thereof provides for a deduction of 2.5% of the credit taken upon removal from factory for home consumption. This gives a cue that the deduction is to be on a flat basis, akin to straight line methodology for grant of depreciation.

"***57S. Manner of utilisation of the capital goods and***

***the credit allowed in respect of duty paid thereon**. - (1) The capital goods in respect of which credit of specified duty has been allowed under Rule 57Q may be -*

(i) used in the factory of the manufacturer of the final products; or
(ii) removed, after intimating the Assistant Commissioner of Central Excise, having jurisdiction over the factory and after obtaining dated acknowledgement of the same, from the factory for home consumption or for export, on payment of appropriate duty of excise leviable thereon or for export under bond, as if such capital goods have been manufactured in the said factory.

(2) In a case,-

(a) where a capital goods are removed without being used from the factory for home consumption, on payment of duty, or for export on payment of duty of excise, 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 rule 57Q:

(b) where capital goods are removed after being used in the factory for home consumption on payment of duty of excise or for export under rebate on payment of duty of excise, such duty of excise shall be calculated by allowing deduction of 2.5 per cent of credit taken for each quarter of a year of use or fraction thereof, from the date of availing credit under rule 57Q;"

15. The CCR 2002 Rules provide as follows with effect from 13.09.2004:

> *" CENVAT credit.*
> *3.(1) A manufacturer or producer of final products shall be allowed to take credit (hereinafter referred to as the CENVAT credit) of--*
> *..........*
> *(4)When inputs or capital goods, on which CENVAT credit has been taken, are removed as such from the factory, the manufacturer of the final products shall pay an amount equal to the duty of excise which is leviable on such goods at the rate applicable to such goods under sub-section (2) of section 3 or section 4 or section 4A of the Act, as the case may be, and such removal shall be made under the cover of an invoice referred to in rule 7."*

16. One issue that has arisen in several cases relating to the reversal of credit relates to the understanding of the phrase 'as such' in the above Rule. While the Department contended that the entirety of the credit availed would have to be reversed, it was the contention of the assessees that such total reversal would only arise if the removal of the goods was in 'as such' condition, that is, without having been put to use.

17. Thus, in cases where the goods had been put to use, a deduction was to be given, to provide for their depreciation. The Appellant has referred to the following cases wherein the issue for consideration touched upon the interpretation of the phrase ‘as such’.

(i) Commissioner of C.Ex Salem V Rogini Mills (264 ELT 367)

(ii) Commissioner of C. Ex Ludhiana V Khalsa Cotspin (P) Ltd (270 ELT 349

(iii) Harsh International (Khaini) Pvt Ltd V Commissioner of Central Excise (281 ELT 714)

(iv) Commissioner of C.Ex Hyderabad V Navodahaya Plastic Industries (298 ELT 541)

18. This Court in the case of *Rohini Mills Limited* (supra) considered the import of the phrase ‘as such’ and rejected the argument of the revenue that the reversal of credit much be total. On a conjoint reading of Rule 3(4) of the 2002 CCR, the 2002 Circular and 1993 Board Letter, the Bench concluded that the assessee was entitled to the benefit of depreciation in arriving at the assessable value of the goods.

19. This decision has also been followed by a larger Bench of

the CESTAT in the case of *Navodhaya Plastic Industries Ltd.* The Bench has, therein, noted the practice of bringing in capital goods for use for a short period and removal to another unit without reversal of CENVAT Credit availed, finding it to be an abuse of the scheme of CENVAT credit. The purpose of the scheme must thus be understood to provide a balance between the grant of credit and checking of abuse in the availment of the same.

20. We are, in this case, not concerned specifically with this issue. There is no dispute that arises qua the parties on the determination of assessable value, save with respect to the aspect of depreciation, specifically, the manner of computation thereof. On the basis of the discussion in the preceding paragraph, it appears apparent that the scheme of credit over the years has provided for a manner of reduction from assessable value by way of Circulars, Letters and the Rules.

21. The 2002 Circular makes reference to the 1993 Board Letter and provides clarifications on various issues relating to the valuation provisions. The relevant portion of the Circular reads thus:

"F.NO. 6/39/2000 – CX 1
Government Of India
Ministry Of Finance
Department Of Revenue
Central Board Of Excise & Customs
Subject : Clarification of doubts under the new Valuation Rules

I am directed to refer to Board's letter F.No. 354/81/2000-TRU dated 30th June 2000 clarifying certain points relating to the new valuation provisions made effective from 1.7.2000.

2. The Board has received a number of references from the field formations as well as representations from the trade associations about certain doubts still persisting in the minds of the field officers. These points of doubt are being clarified in the Table enclosed.

3. Field formations may be suitably informed.

4. Hindi version will follow

5. Receipt of this Circular may kindly be acknowledged.

Sd/-
(A.K.PRASAD)
DIRECTOR (CX I)
3092812

Clarifications on points of doubt under The New Valuation Provisions introduced w.e.f. 1.7.2000
....

14.	*How will valuation be done when inputs or capital goods, on which CENVAT credit has been taken, are removed as such from the factory, under the erstwhile sub rule (1C) of rule 57AB of the Central Excise Rules, 1944, or under rule 3(4) of the Cenvat Credit Rules, 2001 or 2002?*	*Where inputs or capital goods, on which credit has been taken, are removed as such on sale, there should be no problem in ascertaining the transaction value by application of sec.4(1)(a) or the Valuation Rules. [provided tariff values have not been fixed for the inputs or they are not assessed under Section 4A on the basis of MRP]* *There may be cases where the inputs or capital goods are removed as such to a sister unit of the assessee or to another factory of the same company and where no sale is involved. It may be noticed that sub rule (1C) of Rule 57AB of the erstwhile Central Excise Rules, 1944 and Rule3(4) of the Cenvat Credit Rules, 2001(now 2002), talk of determination of value for "such goods" and not the "said goods". Thus, if the assessee partly sells the inputs to independent buyers and partly transfers to its sister units, the transaction value of "such goods" would be available in the form of the transaction value of inputs sold to an unrelated buyer (if the sale price to the unrelated buyer varies over a period of time, the value nearest to the time of removal should be adopted).* *Problems will, however, arise where the assessee does not sell the inputs/capital goods to any independent buyer and the only*

22. The answer to query 14 above, in conclusion, refers to the 1993 Board Letter clarifying the position that the methodology under that Letter, must be applied in the computation of depreciation for ascertainment of transaction value.

23. If this were not to be done, the scheme of grant/reversal of credit would stand distorted as for the period prior to 2002 and subsequent to 2007, the reduction would be computed on a flat rate, on straight line basis whereas for the interim period between 2002 and 2007, the methodology would be different.

24. The stipulation under the 1993 Board Letter has been noted in paragraph 6 above. Though the Board Letter has been issued in the context of second hand motor vehicles, it does provide valuable guidance in regard to the methodology to be followed in computing depreciation and such methodology has been specifically imported in the 2022 Circular as well.

25. On and with effect from 13.11.2007 the following Proviso was inserted in Rule 3(5) of the Cenvat Credit Rules 2004 (in short '2004

CCR') providing for a methodology of deduction I the Rules itself. With this, the ambiguity in regard to the methodology of deduction to be followed stood clarified as it had been incorporated in the relevant Rule.

> *"Provided further that if the capital goods, on which CENVAT Credit has been taken, are removed after being used, the manufacturer or provider of output services shall pay an amount equal to the CENVAT Credit taken on the said capital goods reduced by the percentage points calculated by straight line method as specified below for each quarter of a year or part thereof from the date of taking the CENVAT Credit, namely:-*
> *(a) for computers and computer peripherals:*

for each quarter in the first year @10%
for each quarter in the second year @8%
for each quarter in the third year @5%
for each quarter in the fourth and fifth year @1%

> *(b) for capital goods, other than computers and computer peripherals @2.5% for each quarter.]*

26. According to the appellant, Rule 4(4) of the CCR 2004 would fully support its claim that the reduction from assessable value should be in line with the provision for depreciation under the Income

Tax Act, 1961. In the interests of completion, the above Rule is extracted below:

> *"Conditions for allowing CENVAT credit.*
> *4.(1)...........*
> *(4) The CENVAT credit in respect of capital goods shall not be allowed in respect of that part of the value of capital goods which represents the amount of duty on such capital goods, which the manufacturer claims as depreciation under section 32 of the Income-tax Act, 1961 (43 of 1961)."*

27. We are not in agreement with the appellant that the above Rule would be applicable in the present case. Rule 4 sets out the pre-conditions for availment of credit. One of those conditions is that no credit shall be allowed in respect of that part of the value of capital goods that represents duty amount which the manufacturer claims as depreciation under the Income tax Act 1961.

28. This, by no means, can be understood to relate to Rule 3(4) of the methodology of valuation required thereunder. The reference to depreciation under the Income Tax Act in Rule 4(4) is in an entirely different context and has no application as urged by the Appellant. This

condition has to be seen solely in the context of availment of CENVAT credit only and has no bearing on the valuation of the goods.

29. It would have been another matter altogether if there had been no references otherwise, to the manner of valuation under Rule 3(4). In such a situation, we might have been persuaded to accept the argument that depreciation under the Income tax Act is one of the permissible methods of arriving at the valuation for Rule 3(4).

30. However, the scheme of the grant / reversal of credit, as noted in detail in the paragraphs supra, do give a clear indication as to the stipulated methodology of valuation for the purposes of Rule 3(4). We see no reason to deviate from this methodology which, admittedly, is being followed in a consistent manner.

31. The provision has always been at a flat rate and there has been no option extended to the assessee in regard to the manner by which the depreciation may be computed. In light of this conclusion, the judgement of the Constitution Bench in *Commissioner of Central Excise, Bolpur vs. M/s.Ratan Melting and Wire Industries* (2008 (231) ELT 22

(S.C.) is of no relevance.

32. The substantial questions are answered in favour of the revenue and this appeal is dismissed.

33. In the interests of completion, we refer to yet another series of decisions placed in the compilation relating to the aspect of revenue neutrality. In Commissioner of *C.Ex Jamshedpur V Jamshedpur Beverages* (214 ELT 321), the departmental appeal was dismissed by the Hon'ble Apex Court recording the position that the excise duty paid and modvat credit availed were identical. The question of law raised was kept open.

34. In *Commissioner of C.Ex and Customs Vadodara-II V Indeos ABS Limited* (254 ELT 6288) there is a finding of fact by the CESTAT noted by the Gujaray High Court, that there is identity between the duty paid and credit availed and on that score the appeal was dismissed. Since no arguments have been advanced in this regard and no question of law raised, we make no further reference to this aspect of the matter.

[A.S.M.J.,] & [R.V.J.,]
06.07.2023

NCC :Yes/No
Index :Yes/No
Internet :Yes
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