**Article on liability of 'interest' when CENVAT credit taken wrongly but reversed by an assessee before utilization**

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Before embarking upon to study the scope and implications of the recently issued Circular No. 897/17/2009-CX dated 3.9.2009, by the Central Board of Excise and Customs ('**CBEC**') it is relevant to first understand the scope and purpose of the Cenvat Credit Rules, 2004 (hereinafter '**CCR**'). The Central Government of India had in exercise of its powers conferred by Section 37 of the Central Excise Act, 1944 and Section 94 of the Finance Act, 1994, and in supercession of the Cenvat Credit Rules, 2002 and the Service Tax Credit Rules, 2002, formulated the existing integrated CCR. The primary objective leading to the formulation of the existing CCR was to facilitate and enable the availment of Cenvat Credit at the end of the manufacturer / producer of final products or the provider of taxable services, on the tax paid on the 'inputs' or 'input services' or 'capital goods' used in the course of manufacture or production of a final product or providing any output taxable services. The adoption of this scheme for availment of cenvat credit was also proposed in order to ensure the avoidance of the cascading effect of taxes i.e. tax on tax.

Broadly speaking the CCR scheme prescribes within it the criteria for eligibility, conditions for allowance, list of proper documents, procedure for transfer and distribution, for the purposes of cenvat credit. Hence, in order to appreciate the context of the present Circular it would be important to examine the relevant provisions applicable to it which have been extracted below -

**"Rule 14 of the Cenvat Credit Rules, 2004**

**Rule 14** - ***Recovery of CENVAT credit wrongly taken or erroneously refunded***

*Where the CENVAT credit has been* ***taken or utilized wrongly or has been erroneously refunded****, the same along with interest shall be recovered from the manufacturer or the provider of the output service and the provisions of sections 11A and 11AB of the Excise Act or sections 73 and 75 of the Finance Act, shall apply mutatis mutandis for effecting such recoveries."*

"**Rule 12 of the Cenvat Credit Rules, 2002**

**Rule 12 Recovery of CENVAT credit wrongly taken** –

*Where the CENVAT credit has been* ***taken or utilized wrongly****, the same along with interest shall be recovered from the manufacturer and the provisions of sections 11A and 11AB of the Act shall apply mutatis mutandis for effecting such recoveries.*"

"**Rule 57I of the erstwhile Central Excise Rules, 1944**

**Rule 57I - Recovery of credit wrongly availed of or utilized in an irregular manner –**

*1(i) Where credit of duty paid on inputs has been* ***taken on account of an error, omission or mis-construction,*** *on the part of an officer or a manufacturer or an assessee, the proper officer may, within six months from the date of filing the return as required to be submitted in terms of sub-rule (8) of Rule 57G, and where return as required to be submitted in terms of sub-rule (8) of Rule 57G, and where no such return as aforesaid is filed, within six months from the last date on which such return is to be filed under the said rule, serve notice on the manufacturer or the assessee who has taken such credit requiring him to show cause why he should not be disallowed such credit and where the credit has already been utilized, why the amount equivalent to such credit should not be recovered from him.*

*XXX*

*(5) Notwithstanding anything contained in clause (iii) of sub-rule (1) or sub-rule (3), where credit of duty paid on inputs has been* ***taken wrongly on account of fraud, willful mis-statement, collusion or suppression of facts, or contravention of any of the provisions of the Act or the rules made thereunder*** *with intent to evade payment of duty, the person who is liable to pay the amount equivalent to the credit disallowed, as determined under clause (iii) of sub-rule (1), shall also be liable to pay interest at such rate as may be fixed by the Board under section 11AA of the Act from the first day of the month succeeding the month in which the credit was wrongly taken, till the date of payment of such amount.*

*XXX"*

It can be observed on a plain reading of the above extracted provisions that these are triggered on once cenvat credit is 'taken' or 'utilized' wrongly by an assessee. As far as the language adopted in the above provisions is concerned, it has remained uniform and there hasn't been any significant change in the present provisions from the earlier ones. Under the above provisions both the wrongful 'availment' as well as 'utilization' of cenvat credit have been characterized as distinct and independent categories, both constitute offences and are treated at par for the purposes of the above provisions. However, in order to gather more insight into the above provisions it is relevant to understand the meaning and import of the words 'taken' and 'utilize'. Firstly, the word 'taken', as defined by the Blacks Law Dictionary, means '*to obtain possession or control*[4]' thereby implying the claiming of a right over the credit availed by the assessee while making entries in the records maintained under Rule 9(5) or 9(6) of the said

Rules. Secondly, the word 'utilize', as defined by the Oxford Dictionary, means to '*turn to account / use effectively*[2]' showing a constructive action undertaken by the assessee in order to use or benefit from the use of cenvat credit. It is to be understood here that all of the above cited provisions are penal in nature and even the words used in them are meant to be read in the same manner. Rule 14 of the CCR came under the scanner in a recent decision of the Punjab and Haryana High Court in the case of **Indo-Swift Laboratories Ltd. v. Union of India** reported in **[2009 (240) E.L.T. 328 (P&H)]**. The Hon'ble High Court while being involved in the interpretation of Rule 14 of the CCR observed, "*the said clause has to be read down to mean that where CENVAT Credit has been taken and utilized wrongly, interest should be payable on the Cenvat Credit taken and utilized wrongly. Interest cannot be claimed simply for the reason that the CENVAT Credit has been wrongly taken as such availment by itself does not create any liability of payment of excise duty. On a conjoint reading of Section 11AB of the Act and that of Rules 3 and 4 of the Credit Rules, we hold that interest cannot be claimed from the date of wrong availment of CENVAT Credit. The interest shall be payable from the date CENVAT Credit is wrongly utilized.*"

This decision by the hon'ble High Court of Haryana and Punjab takes cue from its earlier decision in the case of **CCE, Delhi-III v. Maruti Udyog Ltd.** reported in **[2007 (214) ELT 173 (P&H)]** wherein the erstwhile Rule 57I of the Central Excise Rules, 1944 was under consideration. The Hon'ble High Court had in this case held - *the assessee is not liable to pay interest in the case where credit was only taken and not utilized*. Both of the above-said judgments are very significant in nature as this mark an important departure and take into account the nature and object of the cenvat scheme first rather than resorting to a plain reading of the relevant provision. Such an interpretation assumes high significance in the context of availment and utilization of cenvat credit because in the usual course of business an assessee may avail cenvat credit immediately by making a cenvat credit entry in his books but keeps the same hanging for its ultimate utilization towards payment of duty / service tax (or may be to just keep his claim of Cenvat credit alive). This Cenvat credit may also be reversed by the assessee on learning about its non-admissible nature before its utilization.

Now, in regard to the invokability of 'interest', the Hon'ble Supreme Court had in the case of **Pratibha Processors v. UOI**, (**AIR 1997 SC 138)**, observed – "*In fiscal statutes, the import of the words - . - 'tax', 'interest', 'penalty' etc. are well known. They are different concepts. Tax is the amount payable as a result of the charging section. It is a compulsory exaction of money by a public authority for public purposes, the payment of which is enforced by law. Penalty is ordinarily levied on an assessee for some contumacious conduct or a deliberate violation of the*

[1] Blacks Law Dictionary, Bryan A. Garner, 7th ed. (1999) 1466 West Group, U.S.A.
[2] Illustrated Oxford Dictionary, Dorling Kindersley Limited and Oxford University Press, 2007

*provisions of the particular statute. Interest is compensatory in character and is imposed on an assessee who has withheld payment of any tax as and when it is due and payable. The levy of interest is geared to actual amount of tax withheld and the extent of delay in paying the tax on due date. Essentially, it is compensatory and different from penalty - which is penal in character."*

A reading of the above case-law, it is clear that it lays down a fundamental principle of law especially for interpretation of fiscal statutes that, 'interest' should not be equated with penalty since interest is purely compensatory in nature. Hence, in case Cenvat credit is taken in the books by an assessee and is not actually utilized, it would lead to no loss of revenue to the Government by the assessee. This view is more justifiable and eminently fair in its application and upholds the primary objective behind the implementation of the Cenvat scheme which is to facilitate availment of Cenvat Credit. However, the Department preferred an appeal against the above judgment before the Hon'ble Apex Court, which was later dismissed *in limine*.

Against the above backdrop the CBEC entered the arena and in an attempt to clarify the legal position on Rule 14 of the said CCR came out with a Circular No. 897/17/2009-CX, dated 3.9.2009, which read as follows -

"*Since, the Rule 14 of the CENVAT Credit Rules, 2004, is clear and unambiguous in the position that interest would be recoverable when CENVAT credit is* ***taken or utilized wrongly****, it is clarified that the interest shall be recoverable when credit has been wrongly taken, even if it has not been utilized, in terms of the wordings of the present Rule 14.*"

Interestingly, the aforesaid directive of the CBEC has come out as a clarificatory step after the pronouncement of the Supreme Court Order and such other orders on the same issue. As it is evident from the aforesaid Circular dated 03.09.2009, it attempts to distinguish the case delivered by the Hon'ble High Court of Punjab & Haryana in the case of **CCE, Delhi-III v. Maruti Udyog Ltd.** (2007) by observing that the said judgment of the Hon'ble High Court was delivered in the context of the erstwhile Rule 57I of the Central Excise Rules, 1944, therefore the same is not extendable to the present Rule 14 of the CCR. Also, the Supreme Court Order dismissing the Department's appeal *in limine* "*is only a decision and not a judgment*". It is an accepted legal proposition that dismissal of a special leave petition by the Hon'ble Apex Court *in limine* is not a binding precedent and does not constitute law for the purposes of Rule 141 of the Constitution of India, as dismissal of an SLP simply signifies that the case is not found to be fit by the Hon'ble Court and the special leave should not be granted, it does not speak or imply of anything regarding the correctness of the order under appeal. Hence, the Circular stands justified to that extent, but it completely fails to take into account the judgment delivered by the Hon'ble Punjab and Haryana High Court in the case of **Indo-Swift Laboratories Ltd. v.**

**Union of India** (2009) [3] which currently holds the field on the interpretation of Rule 14 of the CCR. In addition to these legal developments the Hon'ble Central Excise and Service Tax Appellate Tribunal (CESTAT) had in the case of **Commissioner of Central Excise, Pondicherry v. Superfil Products** as reported in [2009 (237) E.L.T. 551 (Tri-Chennai)], while being involved with the interpretation of Rule 12 of the Cenvat rules, 2002, observed to the extent that - *the term* ***"taken or utilized"*** *as under Rule 12 of the said Rules should be interpreted as* ***"taken and utilized"***.

Thus, on the basis of the discussion of legal developments it appears that, the stand adopted by the CBEC through its Circular dated 03.09.2009, instead of being clarificatory in nature only confuses the legal position and resorts to a very narrow approach which should be avoided by keeping in sight the objective of the relevant statutes, rules and regulations. As a concluding remark it is highly prudent to conclude by reiterating the observation made by the Hon'ble Apex Court in the case of **Commissioner of C.EX. v. M/s Gujarat Narmada Fertilizers Co. Ltd.** as reported in [2009 (240) E.L.T. 661 (S.C.)] that, ***"Litigation on interpretation of CENVAT Credit Rules has arisen on account of various conflicting decisions given by the various Benches of CESTAT, the reason being that the Rules have not been properly drafted".*** The position becomes worse when the tax administering authority resorts to dishing out interpretations which are more in line with the letter of the law rather than the spirit of it, thereby making the position patently unjust and ethically (if not strictly legally) untenable.



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[3] Citation *supra*