

AMORTARISATION OF COST OF MOULDS AND DIES-TREATMENT UNDER GST LAW

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Clarification

Whether amortisation cost of Dies & Moulds supplied on Free of Cost (FOC) to Components Supplier to be included in the cost of the components for the purposes of levying GST

There is a common practice in manufacturing organizations to outsource manufacturing activities. The manufacturers usually supply Dies or Moulds to outsourced agents in order to maintain quality and integrity of their products. In some cases, such Dies or Moulds are fabricated / manufactured by the outsourced agents at the cost of the manufacturer.

This article deals with the provisions of GST law regarding treatment of the cost of Dies and Moulds in the value of goods produced / outsourced.

Original Equipment Manufacturers (OEM) provide Dies & Moulds to their component supplier (not being related party or distinct person) for the following objectives:

1. The Components Suppliers (CS) may not have access to facilities for making of Dies & Moulds of superior quality to ensure product quality
2. The CS may not be financially capable to bear the cost of Dies & Mould as the recovery of cost will be required to be spread over the projected volumes of finished products of OEM based on product life cycle. For example, cost of making bumper of an automobile may run into crores of rupees and recovery of cost incurred shall be spread over projected volume of that automobile over number of years say 5-10 years
3. Development of critical (depending on complexities of design) Dies & Moulds are a time consuming process hence it may be a business prudence to retain ownership of such Dies & Moulds to safe-guard their interest in case of any CS is not able to supply components due to reasons

attributable to force majeure. In such cases, the OEM may shift such Dies & Moulds.

Let us now examine Section 15 of the CGST Act, 2017 which defines value of taxable supply. Section 15(2) (b) provides that value of supply shall include "any amount that supplier is liable to pay in relation to such supply but which is incurred by recipient of supply and which is not included in price actually paid or payable for the goods or services or both".

The effect of 15(2) is that if any cost which the supplier of the components is required to bear for the supply is borne by recipient then the value of such supply shall include such cost for the purpose of levying Goods & Service Tax (GST).

Question of whether the CS is required to include such a cost/expense as discussed above in the value of supply, shall be determined by the terms of contract between the supplier & recipient –

- (1) If the terms of the contract provide that components/dies/moulds shall be supplied by the recipient then there is no requirement to include the cost of such components or amortized cost of such dies/moulds in the value of supply.
- (2) If the terms of the contract do not provide for any stipulation as specified in (1) above & components/dies/moulds is supplied by the recipient then value of such supply shall include cost of components or amortised cost of dies/tools.

Central Board of Indirect taxes & customs has issued a clarifications on free of cost supply of moulds & dies vide Circular No. 47/21/2018-GST dt 08.06.2018, of which relevant extract is reproduced below:

1.2 It is further clarified that while calculating the value of the supply made by the component manufacturer, the value of moulds and dies provided by the OEM to

the component manufacturer on FOC basis shall not be added to the value of such supply because the cost of moulds/dies was not to be incurred by the component manufacturer and thus, does not merit inclusion in the value of supply in terms of section 15(2)(b) of the Central Goods and Services Tax Act, 2017 (CGST Act for short).

1.3 However, if the contract between OEM and component manufacturer was for supply of components made by using the moulds/dies belonging to the component manufacturer, but the same have been supplied by the OEM to the component manufacturer on FOC basis, the amortised cost of such moulds/dies shall be added to the value of the components.

Though the clarification has been issued by the Central Board of Indirect taxes & customs is related to moulds & dies supplied on Free of cost basis to component manufacturer but it amply clarifies intent of law as contained in section 15(2) for determining the value of supply for the purposes of levy of tax. The terms of contract between the supplier & recipient shall be the basis to determine whether to include the expenses borne by recipient in value of supply or not. If contract provides that expense is to be borne by recipient then there is no requirement to include in the value of supply not otherwise. To illustrate further, let us consider the following example:

A buyer enters into a contract with a component supplier (CS) to supply a product which is manufactured by assembly of several components. The buyer shall be supplying a critical component out of these several components to CS on Free of Cost (FOC basis). The price of the product do not factor the cost of this free component as it is provided by buyer on FOC basis but include the cost of operation performed in using that component. Since the terms of contract is that the components shall be provided by buyer hence pricing of product has been done accordingly. So while supplying this product to buyer (recipient), the cost of FOC component shall not be included in the value of supply.

Now we draw attention to a different scenario where all components are required to be procured by component supplier who being constrained by financial scale economies or infrastructure is not able to procure the same and the components are

supplied by buyer, then the value of the component are to be included in the taxable value of the product to be supplied by CS. This activity will definitely call for re-fixation of price of product as cost of FOC component so received from buyer is already factored in. An alternative procedure in that case may be followed by buyer by supplying such component as taxable supply.