
(2011) 07 DEL CK 0421

Delhi High Court

Case No: CEAR No. 4 of 2004

Commissioner of Central Excise

APPELLANT

Vs

Padmini Polymers

RESPONDENT

Date of Decision: July 7, 2011

Acts Referred:

- Central Excise Rules, 1944 - Rule 173Q(2), 209A, 57A, 57CC(9)
- Central Excises and Salt Act, 1944 - Section 11AB, 14, 5A(1)

Citation: (2011) 187 ECR 406

Hon'ble Judges: Sanjay Kishan Kaul, J; Rajiv Shakdher, J

Bench: Division Bench

Advocate: Satish Kumar, for the Appellant; Pradeep Jain, for the Respondent

Judgement

Rajiv Shakdher, J

1. By an order dated 26.05.2004 in a reference application preferred by the revenue, this Court had directed the Central Excise Service Tax Appellate Tribunal (hereinafter referred to as the "Tribunal") to refer following question of law to this Court:

Whether CEGAT is correct in holding that exemption under Notification No. 4/97-CE dated 01.03.1997 was available to the manufacturer, when statutory provisions contained in Rule 57CC(9) of the Central Excise Rules, 1944 were not followed by the party.

2. Before we proceed further, it would be useful to refer to facts necessary for adjudication upon the question referred to us. These facts being as follows:

2.1 The Respondent/Assessee at the relevant point in time was engaged in the manufacture of articles of plastic falling under chapter sub-heading No. 3923.90 of the schedule to the Central Excise Tariff Act, 1985 (hereinafter referred to as the "Tariff Act"). The Respondent/Assessee in respect of its raw materials being: plastic granules (HDPE, LDPE, Chips); master batches, packing material, etc. used in

manufacture of its finished products, availed of MODVAT Credit under Rule 57A of the Central Excise Rules, 1944 (hereinafter referred to as the "Rules"). Thus, there was a batch of finished goods qua which the Respondent/Assessee paid duty and sought adjustment of duty paid on inputs (i.e., raw material) by seeking recourse to the MODVAT route. There was another batch of finished goods in respect of which the Respondent/Assessee availed of the benefit of exemption notification No. 41/97-CE dated 01.03.1997 (hereinafter referred to as the "exemption notification"), which prescribed "nil" rate of duty for the said finished goods.

2.2 The Respondent/Assessee was, at the relevant time, operating four manufacturing units and was in possession of three godowns. Out of the four manufacturing units, three (3) were located in Sahibabad in the State of U.P. and the fourth (4th) was located in Patparganj in New Delhi. Similarly, out of the three (3) godowns, two (2) were situate in Sahibabad in the state of U.P. which were used for storing finished goods and the third (3rd) godown located in the Wazirpur Industrial Area, Delhi was evidently used for trading plastic granules.

2.3 On, the Directorate of Anti Evasion (DGAE) receiving intelligence that the Respondent/Assessee was clearing goods without payment of duty, a raid was conducted on 07.10.1997 at the various manufacturing units, godowns and registered offices of the Respondent/Assessee.

2.4 According to the revenue, the search carried out at the aforementioned premises of the Respondent/Assessee and the analysis of the records showed several discrepancies, which included excess stock over and above that which was recorded in the stock registers as also presence of raw materials in respect of which documents were not available. The finished goods and raw material found in excess of the quantity shown in the stock registers were seized by the revenue. The Respondent/Assessee as a matter of fact also paid the differential duty in respect of excess stock found in unit Nos. 1 and 2. For the sake of brevity, we are not detailing out herein the discrepancies as they have been set out in the show cause notice issued by the revenue.

2.5 It may only be noted at this stage that the show cause notice dated 02.03.1998 was not filed by the revenue in the captioned appeal. A copy of the same has, however, been handed over by the counsel for the revenue during the course of the hearing.

2.6 In the interregnum, the revenue had recorded the statements of the officers of the Respondent/Assessee u/s 14 of the Central Excise Act, 1944 (hereinafter, referred to as "CE Act"). The statement recorded were those of one Sh. R.K. Chawla, Dy. General Manager (Commercial); Sh. Vijay Gupta, Assistant Manager (Excise); Sh. Vivek Nagpal, Chairman and Managing Director; Sh. Ashok Arora, General Manager; Sh. Raghunath Sharma, Assistant Accounts Manager; Sh. P.K. Jain, Chief Executive Officer, Sh. R.L. Gupta, Assistant Manager; Sh. Rakeshwar Dayal, General Manager

(Purchase) and Sh. Rajneesh Kalra, Assistant Manager (Distribution).

2.7 Since it is necessary for the purpose of adjudication of the question involved, we may briefly advert to the relevant parts of the statement made by each of the officers as recorded in the SCN. It may be noted at this state that the counsel for the Respondent/Assessee has neither disputed the veracity nor the manner in which it has been paraphrased in the show cause notice. Therefore, for the sake of convenience, the same are extracted hereinafter:

R.K. Chawla, Dy. General Manager (Commercial)

Sh. R.K. Chawla further stated that during the year April, 96 to March, 97, they had consumed 6,73,390 kgs and 8,67,158/- kgs. Of raw materials from IV and RG.23A Pt.I respectively for production of exempted goods valued at Rs. 8,36,30,488/- and dutiable goods valued at Rs. 6,48,76,868/-. This had happened because more quantity of raw materials were issued from RG.23A Pt.I, for manufacture of exempted goods. He further stated that same Moulding machines were used for the manufacture of both dutiable and exempted goods, and the above ratio between raw material and finished goods issued from Form IV register and RG-23A clearly shows that modvatable inputs were diverted for the manufacture of exempted goods.

Sh. Vijay Gupta, Assistant Manager (Excise)

He further deposed that though they were accounting for raw materials in RG-23A Pt.I and Form IV Registers for the dutiable and exempted category of goods respectively and the raw materials used for manufacture were accordingly reflected in such records but they were unable to maintain any distinction for identification of these materials as these were not stored separately. As a matter of fact the entire raw materials of particular variety/nature were stored at one place only. He further admitted that they were using the same raw materials for the manufacture of the goods which were being cleared on payment of Central Excise duty as well as under exemption. Similarly, same finished goods which were classifiable under the same tariff were cleared on payment of duty as well as under exemption. The percentage of recovery of duty as well as under exemption. The percentage of recovery of finished goods from the inputs was reported by him to be around 99%. He clearly admitted that benefit of exemption under notification No. 4/97 dated 01.03.97 was not applicable to them. He further deposed that on 07.10.97 there was shortage of finished goods involving Central Excise duty of Rs. 98,975/- which they had voluntarily debited from the PLA.

He further deposed that both modvatable and non modvatable raw material were stored together and as such both category of goods, i.e., dutiable or exempted goods could be manufactured from a particular lot of plastic granules and it also happened in practice. He also stated, inter alia, that they had not entered the receipt of master batches in the Form-IV Register and admitted the mistake.

On perusal of Form IV Register and Rg.23A Pt.I Register for the year 1996-97 he admitted that even though excess quantity of duty paid inputs was issued, yet far less quantity of finished goods, cleared on payment of duty were accounted for in the RG-I Register. Failing to explain this discrepancy, he stated that since both the modvatable and non modvatable inputs were kept together, apparently excess quantity of modvat inputs issued from RG-23A Pt.I were diverted for the manufacture of exempted goods." Sh. Ashok Arora, General Manager "He further stated that they had taken modvat credit on entire master batch and PP bags etc. received in the factories and had entered the same in RG-23 Part I registers although some of these inputs were also used in the manufacture of exempted category of goods.

Vivek Nagpal, Chairman and Managing Director

He also confirmed that there was no segregation of raw materials in respect of which they had availed modvat and those on which they had not availed modvat because of practical difficulties. He also clarified that they maintained Form IV for the raw materials for which no modvat had been availed whereas for modvatable inputs they had maintained RG-23A Pt.I register; and that they had been storing both dutiable and exempted variety of finished products together.

Raghunath Sharma, Assistant Accounts Manager

He further deposed that there was no segregation of dutiable/non dutiable raw materials as well as finished goods, though the records were maintained separately for both modvatable and non modvatable inputs and dutiable and exempted category of finished goods.

P.K. Jain, Chief Executive Officer

He further stated that there was no segregation of either dutiable or exempted variety of raw materials and dutiable or exempted finished goods in as much as both were kept together without any demarcation. He further deposed that master batch and P.P. bags were not entered in Form-IV but both these items i.e., master batch and polybags were used in the manufacture of both dutiable and exempted goods.

R.L. Gupta, Assistant Manager

On 07.10.97, though HDPE granules of Reliance Industries were found in stock, the supporting documents available with the factory were of M/s. IPCL for which he had no satisfactory explanation. He further, agreed with the discrepancies found during stock verification by the visiting DGAE officers and stated that they may not have received exact quantity of raw materials as specified on supporting invoices.

Rakeshwar Dayal, General Manager (Purchase)

Another statement of Shri Rakeshwar Dayal was recorded on 17.10.97, wherein, he inter alia stated that there was no distinction between the modvatable and non modvatable raw materials at the time of its receipt in the factory. In other words, all the raw materials were identical and there were no segregation of raw materials for its utilization in the manufacture of dutiable or exempted category of goods.

Sh. Rajneesh Kalra, Assistant Manager (Distribution)

He agreed with the discrepancies of physical stocks of finished goods.

2.8 As indicted above, a show cause notice was issued . By virtue of the said show cause notice, the Respondent/Assessee was called upon to respond as to why Central Excise Duty amounting to Rs. 7,69,90,751/- ought not to be imposed on the alleged ground of diverting raw material / inputs on which modvat has been availed for the purposes of manufacturing goods cleared at nil rate of duty under the aforementioned exemption notification. In addition, the Respondent/Assessee was also called upon to respond as to why the interest ought not to be levied at the rate of 20% under the provisions of Section 11 AB of the CE Act, as also as regards the proposal to levy penalty under the relevant rules. The Respondent/Assessee was also put to notice with regards to confiscation of seized plastic containers valued at Rs. 68,98,764/- and plastic granules (raw materials) valued at Rs. 1,27,400/-. The show cause notice further proposed appropriation of Rs. 50 Lakhs deposited by the Respondent/Assessee on 22.10.1997 in the form of advance towards excise duty demanded. Furthermore, the Respondent/Assessee was also directed to show cause as to why land, building, plant, machinery, material conveyance and any other thing used in the manufacture, production, storage, removal and disposal of the goods in issue ought not to be confiscated under Rule 173Q(2).

2.9 In so far as Sh. Vivek Nagpal, Chairman and Managing Director and Sh. R.K. Chawla, Dy.GM were concerned, they had been directed to show cause as to why penalty ought not to be imposed on them under Rule 209A.

3. In response to the aforementioned show cause notice, replies were filed by the notices in question which included the Respondent/Assessee. After perusing their reply and hearing their authorized representatives, the Commissioner passed an order-in-original dated 19/21.07.2000. The Commissioner, by virtue of the said order, sustained the submission of the Respondent/Assessee with regard to the fact that there had been no diversion of raw material /inputs in respect of which modvat credit had been availed of in manufacturing finished goods which were cleared by taking recourse to the exemption notification. Thus, proceedings against the Respondent/Assessee(notice No. 1) were dropped with a caveat that seized raw material valued at Rs. 1,27,400/- be confiscated. Option was, however, given to the Respondent/Assessee to redeem the said goods on payment of Rs. 30,000/- as fine in lieu of confiscation. A penalty of Rs. 50,000/- was also imposed. In addition, the Commissioner observed that neither confiscation of plastic containers seized, which

were valued at Rs. 68,98,764/- nor the appropriation of Rs. 50 Lakhs deposited on 20.10.1997 by the Respondent/Assessee was permissible. Proceedings against Sh. Vivek Nagpal, noticee No. 2 and Sh. R.K. Chawla, noticee No. 3 were also dropped.

3.1 The Respondent/Assessee as well as the revenue was aggrieved by the order-in-original passed by the Commissioner. Consequently, two cross-appeals were preferred being appeal Nos. E/1981/01-NB and E/3202/00-NB by the revenue and the Respondent/Assessee respectively, before the Tribunal. In so far as, the Respondent/Assessee was concerned, it did not press its appeal before the Tribunal. Accordingly, the Respondent/Assessee's appeal was dismissed. The appeal of the revenue suffered the same fate, however, after reasons had been supplied for dismissal of the appeal.

3.2 The revenue being aggrieved, sought a reference to this Court, as indicated hereinabove.

4. Before us, submissions on behalf of the revenue were advanced by Mr. Satish Kumar, Advocate while, on behalf of the Respondent/Assessee, arguments were addressed by Mr. Pradeep Jain.

5. Mr. Kumar submitted that the Tribunal had erred in dismissing the appeal of the revenue in as much as it came to the conclusion that the condition prescribed in the exemption notification for keeping "separate inventory" of finished goods which were chargeable to duty and those which were exempted from imposition of duty did not include separate storage. Mr. Kumar submitted that the provisions of Rule 57CC(9) obliged the Respondent/Assessee to store finished goods on which modvat had been claimed separately from those which were cleared by taking recourse to the exemption notification. It was submitted that this was also the understanding of the Respondent/Assessee which is demonstrable from the fact that during the search carried out at the Respondent/Assessee's premises, the revenue obtained copies of undertaking filed by the Respondent/Assessee alongwith classification list and declarations, etc. whereby, it had been undertaken by the Respondent/Assessee that not only will it keep separate records of inputs but would also store those inputs separately, on which, it did not intend to claim modvat but was desirous of clearing the finished goods manufactured with the aid of such inputs by taking recourse to the exemption notification.

5.1 Mr. Kumar submitted that clearly this undertaking was breached; a fact which is borne out from the statement of officers of the Respondent/Assessee recorded by the revenue u/s 14 of the CE Act. In this connection, Mr. Kumar drew our attention to the statements of the concerned officers of the Respondent/Assessee, the relevant portions of which have already been extracted by us hereinabove.

5.2 Mr. Kumar laid emphasis on the statements to show that the inputs on which modvat had been claimed, had been diverted for manufacturing finished goods which were cleared under the exemption notification. Mr. Kumar contended that

even though in the orders of the authorities below, there is a reference to the statements made by the officers, both the Commissioner and the Tribunal have failed to take this crucial fact into account to determine as to whether condition No. 8 of the exemption notification had been breached or not. Mr. Kumar submitted that the authorities below have failed to appreciate this pertinent aspect of the matter and, as a matter of fact have not returned finding in that regard.

6. On the other hand, Mr. Jain took us through the contents of the notification and the orders of the authorities below to emphasis that there was no requirement in law to store separately, the inputs on which modvat had been claimed as against those on which no modvat had been claimed but had been used to manufacture goods which were cleared under the exemption notification. In this regard and with a view to buttress his submission, Mr. Jain also relied upon the judgment of the Supreme Court in the case of [Chandrapur Magnet Wires \(P\) Ltd., Nagpur Vs. Collector of Central Excise, Central Excise Collectorate, Nagpur,](#)

6.1 Mr. Jain vehemently argued that the show cause notice called upon the Respondent/Assessee to answer a charge as to whether the benefit of the exemption notification ought to be denied to the Respondent/Assessee solely on the ground that the Respondent/Assessee had failed to store separately, the inputs on which modvat had been claimed, and those on which no modvat had been claimed but were used to manufacture finished goods which were cleared under the exemption notification. Mr. Jain, in these circumstances, relied upon the judgments of the authorities below and pressed for the dismissal of the revenue's reference.

7. We have heard the learned Counsels for both the revenue and the Respondent/Assessee. In order to understand the contours of the controversy in issue, one would first have to examine in the first instance the relevant terms of the exemption notification. These being as follows:

In exercise of the powers conferred by Sub-section (1) of Section 5A of the Central Excise Act, 1944 (1 of 1944), the Central Government, being satisfied that it is necessary in the public interest so to do, hereby exempts excisable goods of description specified in Column (3) of the Table below or column (3) of the said table read with the relevant list appended hereto, as the case maybe, and falling within the chapter, heading No. or sub-heading No. of the Schedule to the Central Excise Tariff Act, 1985 (5 of 1986), (hereinafter referred to as the said Schedule), specified in the corresponding entry in column (2) of the said table, from so much of the duty of excise leviable thereon which is specified in the said Schedule, as is in excess of the amount calculated at the rate specified in the corresponding entry in column (4) of the said table, subject to any of the conditions specified in the Annexure to this notification, the condition No. of which is mentioned in the corresponding entry in column (5) of the said table.

Condition No.

Condition

8. If no credit of the duty paid on the inputs used in the manufacture of such goods has been availed of by the manufacturer under Rule 57A of the Central Excise Rules, 1944.

(emphasis is ours)

8. In addition to the above, regard would also be required to be had of the provisions of Rule 57CC(9). The said Rule reads as follows:

In respect of inputs (other than inputs used as fuel) which are used in or in relation to the manufacture of any goods, which are exempt from the whole of the duty of excise leviable thereon or chargeable to nil rate of duty, the manufacturer shall maintain separate inventory and accounts of the receipt and use of inputs for the aforesaid purpose and shall not take credit of the specified duty paid on such inputs.

(emphasis is ours)

9. A perusal of the notification would indicate that condition No. 8 clearly stipulates that the benefit of the notification would be available only if in the manufacture of the finished goods, which are cleared under the said notification, those inputs are used on which modvat credit is not claimed under Rule 57A. The obligation to provide separate inventory and accounts of the receipt and use of inputs utilized in the manufacture of exempted finished goods, is contained in the Rules, in particular, Rule 57CC(9). The question which arises is whether the expression "separate inventory" used in Rule 57CC(9) requires physical segregation of inputs on which modvat is claimed and those on which no modvat is claimed and are used in manufacturing finished goods cleared under the exemption notification. The result would turn perhaps on the meaning of the word "inventory". The word "inventory" by itself when compendiously used could refer to not only the raw materials, supplies, finished goods and work-in-progress and merchandise in hand, or in transit and owned, but could also include the aggregate value of such material; the process of counting, listing, pricing and itemizing such material and physical inventory as well (see Dictionary for Accountants ERIC L. KOHLER 5th Edition Page 271). Therefore, the argument made on behalf of the Respondent/Assessee that separate inventory could never include separate storage is not an argument which would find favour with us. We are in fact supported by the observations made by the Supreme Court in this regard in the case of Chandrapur Magnet Wires (P) Ltd. wherein, the Supreme Court while observing that the Assessee ought to have maintained not only "separate accounts" but also "segregated inputs utilized for

manufacture of dutiable goods and duty free goods, allowed the Assessee's appeal on the ground that the Assessee had reversed the credit of duty paid on the inputs used in the manufacture of exempted goods by debiting the credit account before removal of such exempted final products. (see observations made in paragraph 7 at page 161). The purpose of the Rule 57CC(9) is thus, in our view, to facilitate those Assesseees in claiming benefit of exemption notification who do not wish to claim modvat credit.

10. Therefore, in our opinion, the authorities below ought to have understood the purport, scope and effect of condition No. 8 contained in the exemption notification in the background of the provisions of Rule 57CC(9). The entire purpose of incorporating condition No. 8 is that an Assessee cannot be allowed to seek benefit twice over. In other words, the Assessee cannot seek modvat credit on inputs and have that credit adjusted against duty payable against finished goods and, at the same time, utilize those very inputs, on which modvat credit had been claimed for manufacture of finished goods by having them cleared under an exemption notification providing for a nil rate of duty. Therefore, while the Rules provide for maintenance of separate inventory and accounts of receipt and use of inputs which are used in the manufacture of finished goods cleared under the exemption notification as against those on which modvat credit is claimed; the said Rule is not incorporated in the exemption notification. No doubt, for the sake of practicality, convenience and adherence to the Rules, separate storage of inputs used in duty paid finished goods as against exempted finished goods would have gone a long way in avoiding the entanglement, which has arisen in the instant case; the notification by itself did not provide for such physical segregation. The question, however, arises can Rule 57 CC (9) be given a complete go by. In our view, if the Rule had been adhered to, then if a charge of evasion of excise duty had been raised on the same set of facts, the onus would have been on the revenue. Therefore, where the situation is converse, that is, where the Respondent/Assessee fails to physically segregate inputs on which modvat had been claimed and those on which no modvat had been claimed and these inputs were purportedly used for manufacture of finished goods cleared under the exemption notification, the onus would lie entirely on the Respondent/Assessee in order to avail of the benefit of the exemption notification. The authorities below have merely examined the issue from the point of view of the interpretation which according to them, had to be laid on Rule 57CC(9). We are unable to persuade ourselves that this is the correct approach to be adopted in the matter. Notwithstanding the fact that no physical segregation of inputs was carried out by the Respondent/Assessee, it was still open to the Respondent/Assessee based on the records and evidence available in that regard, that it had not used inputs (raw material) for manufacture of finished goods (which were cleared by taking recourse to the exemption notification) on which modvat credit had been claimed. What surprises us is that even though both in the show cause notice as well as in the order of the Commissioner, there is extensive

reference to the statements of the officials and the records, which show prima facie diversion of modvatable inputs for manufacture of goods cleared under the exemption notification, no effort whatsoever has been made to determine as to what is the exact extent of the diversion. The extent of the diversion would have determined the finished goods in respect of which the benefit of the exemption notification had to be denied. In this connection, the argument of Mr. Jain that all the authorities below were required to determine as to whether Rule 57 CC(9) required the Respondent/Assessee to physically segregate the modvatable inputs from those on which no modvat had been claimed and had been used in clearing finished goods under the exemption notification, is in our view misconceived. A bare perusal of the show cause notice would show that it is replete with allegations that Respondent/Assessee diverted modvatable inputs in manufacture of exempted finished goods. There is not even a finding that such an exercise was attempted and the Respondent/Assessee failed to provide the relevant evidence and material in that regard to determine the extent of diversion and hence, in the final analysis failed to discharge its onus in that regard. In these circumstances, the impugned judgment of the Tribunal dated 12.09.2002 is set aside and the matter is remanded to the Commissioner to determine the exact extent of diversion of modvatable inputs by the Respondent/Assessee in the manufacture of goods cleared during the relevant period by seeking recourse to the exemption notification.

11. This exercise shall be completed by the Commissioner within the period of three months from today after giving the opportunity both to the Respondent/Assessee as well as the revenue.

The reference is answered accordingly.