Union of India and Others

Vs

M/S Playworld Electronics Pvt. Ltd. and Another

Civil Appeal No. 859 (Nm) of 1988

(S. Ranganathan, Sabyasachi Mukharji JJ)

02.05.1989

JUDGMENT

SABYASACHI MUKHARJI, J. –

1. This is an appeal by special leave from the judgment and order of the High Court of Delhi dated January 12, 1988.

2. The respondent company manufactured wireless receiving sets, tape recorders, tape players which were assessable under Tariff Items 33-A and 37-AA of the Central Excise Tariff and it had filed a classification list and price lists in respect of the said goods. On verification of the said lists, it was found that the goods were unbranded and on investigation it was alleged to have come to the notice of the department that the respondent company was engaged in the manufacture of wireless receiving sets and tape recorders in the brand name of "Bush". From the documents filed by the respondent, according to the appellants, it was revealed that the respondent manufactured their entire products in the brand name of "Bush" from the very beginning and were selling the same exclusively to M/s. Bush India Limited or its authorised wholesale dealers only. This fact was nowhere mentioned by the respondent in its price list or its classification lists and this, according to the appellants, amounted to wilful suppression of facts with the intention to evade payment of central excise duty. Certain enquiries were made and to safeguard the interest of revenue the respondent was requested time and again to observe the provisions of Rule 9-B of the Central Excise Rules, 1944 and execute B-13 surety bond. However, it is stated that the respondent evaded the execution of the said bond which was, according to the appellants, done deliberately. Thereafter, on January 4, 1985, a show cause notice was issued for the period April 1, 1983 to November 30, 1984 requiring the respondent to show cause as to why M/s. Bush India Limited should not be treated should not be treated as a related person and a favoured buyer of the respondent company for the purpose of determination of wholesale cash price and as to why the concessional rate of duty under Notification No. 358/77-CE should not be denied to the respondent and as to why the differential duty in respect of the goods cleared during the period should not be recovered. While the adjudication on the basis of the show cause notice was pending, the respondent company was again requested to execute the surety bond in July, 1984. Respondent company thereafter filed a writ petition in the High Court of Delhi under Article 226 of the Constitution praying for quashing of the show cause notice and the communication dated July 11, 1984 and for a mandamus to allow it to clear the goods on the basis of the price at which the goods were sold by it allowing the benefit of the relevant notification. The High Court by the order dated January 12, 1987 held that the value of the goods manufactured by the respondent company was the price charged by it from M/s. Bush India Ltd. and not the market value at which M/s. Bush India Ltd. sold the goods to its wholesalers. In the premises, it was held that there was no misdeclaration of the value and the show cause notices

were quashed. In passing the impugned order, the High Court followed its decision in C.W. 197 of 1985. It is, therefore necessary to refer to the said decision of the High Court. The said decision challenged the notice dated December 31, 1984 and a demand notice of the same date. It was contended on behalf of the petitioner in that case, who is the respondent in the instant appeal that the said respondent merely manufactures the aforesaid item for Bush India and after manufacturing those, it sells those to M/s. Bush India Ltd. It was contended that, for the purpose of finding out the price for payment of excise duty only the price which was charged by the respondent from Bush India Limited could be taken into account and the price at which M/s. Bush India Limited further sold those goods in the market was not the price which was to be taken for the purpose of excise duty. It was contended that Bush India Limited was not a related person of the respondent within the meaning of Section 4(4)(c) of the Central Excises and Salt Act, 1944 (hereinafter referred to as 'the Act') and reliance was placed on the decision of this Court in Union of India v. Bombay Tyre International ((1984) 1 SCC 467 : 1984 SCC (Tax) 17 : (1984) 1 SCR 347). On the merits of the case, reliance was also placed on certain decisions of this Court as well as the decision of the Delhi High Court. The High Court found that the case of the respondent was directly covered by all these decisions. In the premises, the High Court quashed the said show cause notices and the demand notice. The question, therefore, is whether the High Court was right in the view it took.

3. Unfortunately, in the instant case, apart from the facts recorded hereinbefore, there is no other fact. Learned counsel appearing for the revenue, Shri A. Subba Rao contended before us that the High Court was in error in not realising that in the facts and the circumstances of this case, it was an arranged affair and that really M/s. Bush India Ltd. was a related person and as such the price charged from it could not represent the correct assessable value for the purpose of excise duty.

4. As noted hereinabove, the events in this case happened from 1985 onwards. In the premises, the amended provisions of section 4 of the Act, as amended by the Amendment Act of 1973, would be applicable. Section 3 of the said Act enjoins that there shall be levied and collected in such manner as might be prescribed duties of excise on all excisable goods other than salt which are produced and manufactured in India. Section 4(1)(a) of the Act provides :

> 4(1) Where under this Act, the duty of excise is chargeable on any excisable goods with reference to value such value shall, subject to the other provisions of this section, be deemed to be -
>
> (a) the normal price thereof, that is to say, the price at which such goods are ordinarily sold by the assessee to a buyer in the course of wholesale trade for delivery at the time and place of removal, where the buyer is not a related person and the price is the sole consideration for the sale :
>
> Provided that -
>
> (i) where, in accordance with the normal practice of the wholesale trade in such goods, such goods are sold by the assessee at different prices to different classes of buyers (not being related persons) each such price shall, subject to the existence of the other circumstances specified in clause (a), be deemed to be the normal price of such goods in relation to each class of buyers;

5. Proviso (iii) to Section 4(1)(a) of the Act enjoins that :

where the assessee so arranges that the goods are generally not sold by him in the course of wholesale trade except to or through a related person, the normal price of the goods sold by the assessee to or through such related person shall be deemed to be the price at which they are ordinarily sold by the related person in the course of wholesale trade at the time of removal, to dealers (not being related persons) or where such goods are not sold to such dealers, to dealers (being related persons) who sell such goods in retail.

6. According to clause (c) of sub-section (4) of Section 4 of the Act, "related person" means a person who is so associated with the assessee that they have interest, directly or indirectly, in the business of each other and includes a holding company, a subsidiary company, a relative and distributor of the assessee, and any sub-distributor of such distributor. The Explanation to section 4(4)(c) further provides that in this clause "holding company", "subsidiary company" and "relative" have the same meaning as in the Companies Act, 1956 (1 of 1956). It is in this context that the validity or otherwise of the High Court's view has to be judged.

7. In Union of India v. Bombay Tyre International ((1984) 1 SCC 467 : 1984 SCC (Tax) 17 : (1984) 1 SCR 347) this Court had to examine this question. This Court examined the scheme of section 4(1)(a) before the Amendment Act, 1973, and also the position after the amendment. It was contended in that case before this court that the definition of the expression "related person" was arbitrary and it included within its ambit a distributor of the assessee. This Court however held that in the definition of "related person" being a relative and a distributor could be legitimately read down and its validity upheld. The definition of related person should be so read, this Court emphasised, that the words "a relative and a distributor of the assessee" should be understood to mean a distributor who was a relative of the assessee. The Explanation to section 4(4)(c) provides that the expression "relative" has the same meaning as in the Companies Act, 1956. The definition of "related person", as being "a person who is so associated with the assessee that they have interest, directly or indirectly, in the business of each other and includes a holding company, a subsidiary company..... ", shows a sufficiently restricted basis for employing the legal fiction. This Court reiterated that it is well settled that in a suitable case the court could lift the corporate veil where the companies share the relationship of a holding company and a subsidiary company and also to pay regard to the economic realities behind the legal facade. The true position, it was explained by the aforesaid decision, under the said Act is - the price at which the excisable goods are ordinarily sold by the assessee to a buyer in the course of wholesale trade for delivery at the time and place of removal as defined in sub-section (4)(b) of section 4 of the Act is the basis for determination of excisable value provided, of course, the buyer is not a related person within the meaning of sub-section (4)(c) of Section 4 and the price is the sole consideration for the sale. This aspect was further examined by this Court in Union of India v. Atic Industries Ltd. ((1984) 3 SCC 575 : 1984 SCC (Tax) 217 : (1984) 3 SCR 930). This Court referred to the decision of Bombay Tyre International ((1984) 1 SCC 467 : 1984 SCC (Tax) 17 : (1984) 1 SCR 347) and also referred to the first part of the definition of "related person" in clause (c) of section 4(4) which defines "related person" to mean "a person who is so associated with the assessee that they have interest directly or indirectly in the business of each other". It was not enough, it was held, that the person alleged to be a related person had an interest, direct or indirect in the business of the assessee. To attract the applicability of the first part of the definition, the assessee and the person alleged to be a related person must have interest direct or indirect in the business of each other. Each of them must have a direct or indirect interest in the business of the other. The quality and degree of interest which each has in the business of the other may be different; the interest of one in the business of the other may be direct while the interest of the latter in the business of the former may be indirect. That would

not make any difference so long as each has got some interest, direct or indirect in the business of the other. In that case, this Court found that Atul Products Ltd. had interest in the business of M/s Atic Industries Ltd. since it held 50 per cent of the share capital of that assessee and had interest as shareholder in the business carried on by the assessee. But this Court was of the view that it could no be said that the assessee, a limited company, had any interest, direct or indirect in the business carried on by one of its shareholders, namely, Atul Products Ltd., even though the shareholding of such shareholder might be 50 per cent. Secondly, it was noted that Atul Products Ltd. was a wholesale buyer of the dyes manufactured by the assessee but even then, since the transaction between them as principal to principal, it was difficult to appreciate how the assessee could be said by virtue of that circumstance to have any interest, direct or indirect, in the business of Atul Products Ltd. The assessee, it was observed, was not concerned whether Atul Products sold or did not sell the dyes purchased by it from the assessee nor was it concerned whether Atul Products Ltd. sold such dyes at a profit or at a loss. In those circumstances, the first part of the definition of related persons in clause (c) of sub-section (4) of section 4 of the amended Act was, therefore, clearly not satisfied both in relation to Atul Products Ltd. as also in relation to Crescent Dyer and Chemicals Ltd., a subsidiary company of Atic Industries Ltd., and neither of them could be said to be a "related person" vis-a-vis the assessee within the meaning of the definition of that term in clause (c) of sub-section (4) of Section 4 of the amended Act. In those circumstances, the assessable value, it was held, of the dyes manufactured by the assessee could not be determined with reference to the selling price charged by Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. to their purchasers but must be determined on the basis of the wholesale cash price charged by the assessee to Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. In that case, the assessee at all material times sold the large bulk of dyes manufactured by it in wholesale to Atul Products and Imperial Chemical Industries (India) Pvt. Ltd. which subsequently came to be known as Crescent Dyes and Chemicals Ltd. at a uniform price applicable alike to both these wholesale buyers and these wholesale buyers sold these dyes to dealers and consumers at a higher price which inter alia included the expenses incurred by them as also their profit. It was noted that the transactions between the assessee on the one hand and Atul Products Ltd. and Crescent Dyes and Chemicals Ltd. on the other were as principal to principal and the wholesale price charged by the assessee to Atul Products Ltd. and Crescent Dyes and Chemicals was the sole consideration for the sale and no extra-commercial considerations entered in the determination of such price. For appreciating how the wholesale price could be the basis of the determination of the assessable value, a reference may by made to the decision of this Court in Union of India v. Cibatul Limited ((1985) 4 SCC 535 :1986 SCC (Tax) 66 : Supp 3 SCR 95). In that case, the respondent, Cibatul Ltd. entered into two agreements with Ciba Geigy of India Ltd. for manufacturing resins by the seller. The joint manufacturing programme indicated that the resins were to be manufactured in accordance with the restrictions and specifications constituting the buyer's standard and supplied at prices to be agreed upon from time to time. The buyer was entitled to test a sample of each batch of the goods and after its approval the goods were to be released for sale to the buyer. The products were to bear certain trademarks being the property of the foreign company - Ciba Geigy of Basle. Tripartite agreements were also executed between the buyer, the seller and the foreign company, recognising the buyer as the registered or licensed user of the trade marks, authorising the seller to affix the trade market on the products manufactured "as an agent for and on behalf of the buyer and not of his own account" and the right of the buyer being reserved to revoke the authority given to the seller to affix the trademarks. The respondent in that case filed declaration for the purpose of levy of excise under the said Act showing the wholesale prices of different classes of goods sold buy it during the period May 1972 to May 1975. The declaration included the wholesale price of the different resins manufactured under the two aforesaid agreements. The Assistant Collector of Customs revised those

price upwards on the basis that the wholesale price should be the price for which the buyer sold the product in the market. According to the Assistant Collector the buyer was the manufacturer of goods and not the seller. The Collector of Central Excise allowed the appeals of the respondent and accepted the plea that the wholesale price disclosed by the seller was the proper basis for determining the excise duty. The appellate orders were, however, revised by the Central Government under sub-section (2) of Section 36 the Act and the orders made by the Assistant Collector were restored. According to Central Government the buyer was the person engaged in the production of the goods and the seller merely manufactured them on behalf of the buyer and that, under the agreements the seller was required to affix the trademarks of the buyer on the manufactured goods and that indicated that the goods belonged to the buyer. There is a ring of similarity between the facts of that case and the facts of the instant appeal before us. The orders of the Central Government were challenged under Article 226 of the Constitution. The High Court held that the goods were manufactured by the seller as its own goods, and therefore, the wholesale price charged by the seller must form the true basis for the levy of excise duty. On appeal, this Court held that the High Court was right in concluding that the wholesale price of the goods manufactured by the seller was the wholesale price at which it sold those goods to the buyer, and it was not the wholesale price at which the buyer sold those goods to others. The relevant provisions of the agreements and the other material on the record showed that the manufacturing programme was drawn up jointly by the buyer and that the buyer and the seller and not merely by the buyer, and that the buyer was obliged to purchase the manufactured product from the seller only if it conformed to the buyer's standard. For this purpose, the buyer was entitled to test a sample of each batch of the manufactured product and it was only on approval by him that the product was released for sale by the seller to the buyer. It was apparent that the seller could not be said to manufacture the goods in those facts, it was held, on behalf of the buyer. It was further found that it was clear from the record that the trademarket of the buyer were to be affixed on those goods only which were found to conform to the specifications or standard stipulated by the buyer. All goods not approved by the buyer could not bear those trade marks and were disposed of by the sellers without the advantage of those trademarks.

8. This question was again examined by this Court in Joint secretary to the Govt. of India v. Food Specialities Ltd. ((1985) 4 SCC 516 : 1986 SCC (Tax) 47 : 1985 Supp 3 SCR 165). There the respondent used to manufacture certain goods for sale in India by M/s Nestle's Products India Ltd. (For short Nestle's) under certain trademarks in respect of which the latter was registered as the sole registered user in India. The goods were supplied to Nestle's at wholesale price on rail at Moga or free on lorry at factory. The respondent disputed the value of the goods determined by the excise authorities for the purpose of the levy under the said Act and ultimately the respondent filed writ petitions in the High Court. The High Court allowed the writ petitions holding that the value of the trademarks could not form a component of the value of the goods for the purpose of assessment of excise duty. In appeal to this Court the appellant contended that the value of the goods sold by the respondent to Nestle's should, for the purpose of levy of excise duty, include the value of the trademarks under which the goods were sold in the market and that the value of such trademarks should be added to the wholesale price for which the goods were sold by the respondent to Nestle's. Dismissing the appeal, it was held that the value of Nestle's trademarks could not be added to the wholesale price charged by the respondent to Nestle's for the purpose of computing the value of the goods manufactured by the respondent in the assessment to excise duty. In that case, it was held that what were sold and supplied by the respondent were goods manufactured by it with the trademarks affixed to them and it was the wholesale cash price of goods that must determine the value for the purpose of assessment of excise duty. It was immaterial that the trademarks belonged to Nestle's.

What was material was that Nestle's had authorised the respondent to affix the trademarks on the goods manufactured by it and it was the goods with the trademarks affixed to them that were sold by the respondent to Nestle's. There could, therefore, be no doubt, it was held, that the wholesale price at which the goods with the trademarks affixed to them were sold by the respondent to Nestle's as stipulated under the agreements would be the value of the goods for the purpose of excise duty. That was the price at which the respondent sold the goods to Nestle's in the course of wholesale trade.

9. Similarly in the instant case, it appears that the brand name "Bush" was affixed to the goods produced by the respondent. In M/s. Sidhosons v. Union of India ((1987) 1 SCC 25 : 1987 SCC (Tax) 68), it was held that the excise duty was payable of the market value fetched by the goods, in the wholesale market at the factory gate manufactured by the manufacturers, i.e., the price charged by the manufacturers to the buyer under the agreement. It could not be assessed on the basis of the market value obtained by the buyer who also add to the value of the manufactured goods the value of their own property in the goodwill of the 'brand name'.

10. In view of the facts that have emerged in this case, the High Court came to the conclusion that the market value of the goods of the respondent herein was the price charged from M/s Bush India Limited and not the market value at which price M/s Bush India Limited sold to its wholesalers for the purpose of payment of excise duty. The High Court, therefore, quashed the show cause notice and the demand notice.

11. Shri A. Subba Rao on behalf of the revenue tried to contend before us that the facts of this case revealed that it was a device to undercharge. The respondent herein was brought in to divide the sale price of M/s Bush India Limited to be basis of the assessable value. It is true that the facts of this case do warrant a great deal of suspicion. But it is not possible to hold otherwise than what has been held by the High Court in this case. It is true, as Shri Rao drew our attention, that even though the corporation might be a legal personality distinct from its members, the court is entitled to lift the mask of corporate entity if the conception is used for tax evasion, or to circumvent tax obligation or to perpetrate a fraud. In this connection, reference may be made to the observations of this Court in Juggi Lal Kamlapat v. CIT ((1969) 1 SCR 988 : AIR 1969 SC 932 : 73 ITR 702). In the background of the facts found we, however, need not get ourselves bogged with the controversy as to the judicial approach to tax avoidance devices as was pointed out in McDowel and Co. Ltd. v. CTO ((1985) 3 SCC 230 : 1985 SCC (Tax) 391 : (1985) 154 ITR 148), where this Court tried to discourage colourable devices. It is true that tax planning may be legitimate provided it is within the framework of the law. Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid the payment of tax by dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges. It is also true that, in order to create the atmosphere of tax compliance, taxes must be reasonably collected and when collected, should be utilised in proper expenditure and not wasted. (See the observations in CWT v. Arvind Narottam ((1988) 4 SCC 113 : 1988 SCC (Tax) 477).) It is not necessary, in the facts of this case, to notice the change in the trend of judicial approach in England (Sherdley v. Sherdley ((1987) 2 All ER 54)). While it is, as observed by Chinnappa Reddy, J. in McDowel and Co. Ltd. v. CTO ((1985) 3 SCC 230 : 1985 SCC (Tax) 391 : (1985) 154 ITR 148) too much to expect the legislature to intervene and take care of every device and scheme to avoid taxation and it is up to the court sometimes to take stock to determine the nature of the new and sophisticated legal devices to avoid tax and to expose the devices for what they really are and to refuse to give judicial benediction, it is necessary to remember as observed by Lord Reid in Greenberg v. IRC ((1971) 47 RC 240 : 1972 AC 109 (HL)) that one must find out the true nature of the transaction. It is unsafe to make bad laws out of hard facts and one should avoid subverting the

rule of law. Unfortunately, in the instant case, facts have not been found with such an approach by the lower authorities and the High Court had no alternative on the facts as found but to quash the show cause and the demand notices.

12. In that view of the matter, the appeal fails and is, accordingly dismissed. But there will be no order as to costs. We dismiss this appeal with reluctance. Our reluctance is not to be ascribed to any hesitation to accept the inference flowing from the facts found but reluctance is due to the facts that the facts were not properly found.

</html