V. S. T. Industries Ltd

Vs

Collector of Central Excise, Hyderabad

(CJI J. S. Verma, B. N. Kirpal, V. N. Khare JJ)

08.01.1998

JUDGEMENT

Kirpal J.

1.These appeals involve for decision the question whether notional interest on the interest free security deposit received should be considered for the purpose of arriving at the assessable value under the Excise Act by including interest at the rate of 12% per cent per annum on such security deposits.

2.V.S.T. Industries Ltd.(appellant in CA No.2524/92) is a company carrying on business of manufacture and sale of cigarettes which was assessable to duty under the erstwhile Item No.4 of the First Schedule to the Central Excise and Salt Act, 1944.The other two appellants, namely, Venus Tobacco Company Pvt.Ltd.(appellants in CA No.2523/92) and Hyderabad Deacon Cigarette Factory Ltd.(appellant in CA No.2611/92) are also cigarette manufacturers and use their plant and machinery to manufacture cigarettes for and on behalf of VST Industries Ltd.(hereinafter referred to as "VST").The question involved in these appeals, therefore, relates to the fixation of the assessable value of the cigarettes manufactured and sold under the brand name owned by VST.

3.The undisputed facts are that the cigarettes manufactured by the appellants are sold in wholesale, exfactory, at cum-duty prices to main dealers who buy these cigarettes on a principal-to-principal basis. The main dealers in turn sell the cigarettes to other wholesale dealers called sub-dealers who in turn sell these cigarettes to the retailers. The cigarettes were being sold by the appellants either on cash-and-carry basis or by extending credit facilities to few of the main dealers. As the appellant company, namely, VST found that several of the main dealers were taking considerable time in making remittances for cigarettes which were delivered to them, they issued a circular dated 22nd September, 1981 whereby it introduced credit facility if interest free security deposits were made with the company. In the said circular it was written that "with a view to provide the facility of suchey do not want to make the security deposit. The company reserves the right to apply the amount of security deposit towards payment of unpaid price or any other amounts which may be due to the buyer to the company or any account whatsoever. On discontinuation of trading with the buyer the company will return the security deposit or the balance if any remaining after the company has deducted/adjusted any amount due to the company by the buyer on any account whatsoever and this will be strictly without prejudice to and in addition to the company's other right. A copy of the revised conditions of sale for cigarettes effective from October 1, 1981 are annexed herewith. In the event of your desiring to avail yourself of the credit facilities kindly send a letter as per the form enclosed for your convenience."

4.A show cause notice dated 28th December, 1987 was issued from the office of the Collector of Central Excise to the appellants. In the said notice it was, inter alia, stated that the receipt of security deposits by VST from the main dealers and without payment of interest would influence the sale price of it's cigarettes to these main dealers. It was accordingly proposed to work out a notional interest at the rate of 12 per cent on the sums of security deposits received by VST from the main dealers and to add this to the sale price of the cigarettes so as to re-determine the assessable value as well as differential duty payable for the cigarettes cleared by the company during the above period. This was proposed on the ground that the sale price of the cigarettes by VST dealers did not constitute the normal price under Section 4 of the Central Excise and Salt Act and in such a situation where an additional money consideration has been there between the parties concerned, the normal price had to be determined only under Rule 5 of the Valuation Rules, 1975.The said show cause notice also referred to the receipt of the freight service charges by the appellants, but in these appeals we are not concerned with that question.

5.Reply was sent to the said show cause notice regulating the claim of the excise authorities. VST while denying its liability paid the demand of Rs.2,23,10,405.79 under protest. The other two appellants, namely, Venus Tobacco Company Pvt.Ltd. and Hyderabad Deacon Cigarettes Factory Ltd. similarly paid Rs.3,92,864.89 and Rs.18,84,718.74 respectively.

6.On the 17th March, 1988 the Assistant Collector of Central Excise passes an adjudication order against VST Industries Ltd. and confirmed the demand of Rs.2,23,10,405.79.Similar orders were also passed against other two appellants by their respective Assistant Collectors of Central Excise. All the three appellants then filed appeals. The collector of Central Excise(Appeals) passed an order on 19th August, 1988 whereby he set aside that part of the Assistant Collector's order which sought to add notional interest to security deposits for reworking the assessable value, while confirming the addition of the freight service charges.

7.The excise authorities then filed appeals against the deletion of the notional interest from the assessable value. The tribunal allowed the department's appeal holding that notional interest charges should be considered for arriving at the assessable value of cigarettes but such extra commercial consideration should be added to price and not assessable value. It is against this decision of the Tribunal that the present appeals have been filed.

8.On behalf of the appellants it was contended by Shri Anil B.Divan, learned senior counsel, that the wholesale price which was charged by the appellants was not in any way influenced by the security deposit which some of the dealers had made who wanted to get goods on credit. He submitted that the transactions with the dealers were on principal-to-principal basis and the appellants charged a uniform price from all dealers, irrespective of the fact whether the sale was made on cash basis or on credit. He drew attention to the latest circular issued by the Central Board of Central Excise and Customs dated 27th May, 1996 in which it was, inter alla, stated that the Ministry of Law had advised that if there was no nexus between the security deposit/advance made by the wholesale buyer and the sale price of the excisable goods or if the department is not in a position to determine the money value of the additional consideration, the provisions of Rule 5 of Central Excise(Valuation) Rules, 1975 would not be applicable. The circular further stated that normally "where the same price is charged from buyers who have given the deposit and from those who have not given the deposit and/or where the advance is purely a security deposit and the interest earned by such deposit is credited to the buyer the notional interest on such advance cannot be added to the price."

9.Refuting the aforesaid submission Shri N.K.Bajpai, learned counsel for the respondent, submitted that the appellants gained considerable pecuniary advantage by having received interest free security deposit. The receipt of this deposit must be taken into account in determining the assessable value. He contended that Rule 5 of the Central Excise is applicable because price was not the sole consideration and the value of such goods has to be based on the aggregate of the price and the amount of notional interest on the security deposit received by the appellants. In support of his submission strong reliance was placed on the decision of this Court in the case of Metal Box India Ltd.Vs.Collector of Central Excise, Madras (1995) 2 SSC 90).

10.Before referring to the decision in Metal Box's case it will be appropriate to refer to other decisions which are relevant on the point in issue which are Collector of Central Excise Vs.Indian Oxygen Ltd.(1988(36) E.L.T 730(S.C.) and Government of India Vs.Madras Rubber Factory Ltd.(1995(77) E.L.T 433(S.C.)) In Indian oxygen case two questions which arose for consideration were whether rental charges for gas cylinders and interest earned on deposit made for several return of gas cylinders, whether interest be notional or actual, could be included in determining the assessable value. It was observed by this Court as follows:

> "It is well settled that the levy under the Act, is on the manufacture. Under Section 4(I)(a) of the Act, excise duty 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 the normal price thereof, that is to say, the price at which such goods are ordinary sold by the assessee to a buyer in the course of wholesale trade for delivery is not a related person and the price is the sole consideration for the sale. Here the sale is of the gases. The levy is on the manufacture of gases and the excisable goods are these gases. "It was held that the supply of gas cylinders was ancillary to the supply of gases. It was open to the customers to bring their own cylinders and deposit was required to be given only if the customers required the company to lend the cylinders. The activity of giving cylinders was held to be ancillary and profits and gains from the deposit so received was not required to be taken into account while computing the value of the excisable goods. It had also been contended on behalf of the Revenue that there were two different classes of buyers; one class of such buyers was that who used to bring their own cylinders and the other who used to get supply of gases from the cylinders of the suppliers. It was, therefore, submitted that different rates for these two classes of buyers constituted two different markets which was permissible under Section 4.Dealing with this contention it was observed at page 732 as follows:

"There may be different classes of buyers for different classes of goods. Section 4(1)(a) of the Act emphasizes that if the goods is of the same type, the prices should also be the same. The proviso to the said Section postulates that where in accordance with normal practice such goods, namely, the gases are sold to different classes of buyers then different prices may be charged. If gases had been sold to different classes of buyers at different rates, it is possible that there might be different markets for the same. But here the charges like rentals for the cylinders and the notional interest income, are for ancillary or allied services and that is not an activity of manufacture. Hence Section 4(1)(a) proviso can be of no avail to that revenue."(emphasis added)

In Madras Rubber Factory case (supra) this Court analyzed Section 4 and observed as under:

> "It is obvious that the value of excisable goods for the purpose of sub-section (1) of

Section 4 is ordinarily determined with reference to the normal price at which such goods are sold, i.e. under clause (a) of sub-section (1) of Section 4.Only where the goods are not sold, and therefore, the price of such normal price of such goods is not ascertainable or in a situation where the normal price of such goods is not ascertainable for some other reason that clause(b) is attracted, where under the nearest ascertainable equivalent price is ascertained in accordance with the rules framed in that behalf. Clause (b) is in the nurture of a residuary clause which should be resorted to where the normal price cannot be ascertained for the reasons mentioned therein. In other words, where the normal price is available or is ascertainable, resort to clause (b) is not permissible. "It then considered as to what are the various deductions from the price received which were permissible in order to arrive at the assessable value. One of the amounts claimed as a deduction from the amount received by the manufacturer was the element of interest received by it on the goods sold on credit. Dealing with this the Court at Page 470 observed as under:

"The case of the assessee(Madras Rubber Factory) is that where the goods are sold to up-country wholesale buyers and payments are received quite sometime later, it is indeed a case of sale on credit and, therefore, the interest charged from the date of delivery of goods till the date of realisation of the price thereof should be deducted from the value of goods. The interest charged, it is submitted, is only in lieu of the time-taken in making the payment by the up-country wholesale buyer. Since this is the amount received subsequent to the sale from the depots and does not fall within the ambit of any of the expenses held ineludible in Bombay Tyre International, it is clearly excludible. The claim for the deduction is, therefore, allowed. "The aforesaid observations clearly show that when goods are sold on credit and interest is received that does not form part of the price on which excise duty is payable.

11.Coming to the facts of the present case it is not in dispute that the appellants are charging a uniform price from there wholesale dealers. The price at which the cigarettes are sold at the factory gate was the same irrespective of the fact whether the dealers were buying the cigarettes on credit or against payment of money. As is indicated in the circular, and there is no dispute to what has been stated therein, one of the commercial considerations for introducing interest free deposit scheme was to cover the risk of credit sales extended to bulk customers. There is nothing on the record to show that the receipt of the deposit from some of the dealers could possible influence the fixation of the sale price even with regard to those sales which were made at the factory against cash and not on credit. Had there been a difference in the selling price where, for example, special discount was given to the dealers who had given a deposit then it may have been possible to say that there were two different markets and two different prices and that lesser price was being charged for an extraneous consideration and, in such a case the notional or actual interest could be added. But that is not the case here. Metal Box case (supra) was the one where two different prices were being charged. In Metal Box case the assessee was manufacturing goods which were offered for sale to M/s.Ponds India Ltd. a wholesale buyer, who required bulk of the containers manufactured by the assessee for marketing its cosmetic products. In order to ensure a steady and regular supply Ponds India Ltd. gave large advance and an agreement had been entered into between the parties as a result whereof discounts were given by the assessee to Ponds India Ltd. which were to be deducted from the gross price. This deduction was not allowed by the excise authorities and the Tribunal.It was contended on behalf of the assessee in this Court that the Tribunal erred in restoring the loading of purchase price by the ad hoc interest on advances made by Ponds India Ltd. to the assessee. While rejecting this contention this Court took notice of the fact that Ponds India Ltd. was a wholesale

buyer who was lifting ninety per cent of the total production of the appellant. The assessee was giving to Ponds India Ltd. fifty per cent discount from normal price and Ponds India Ltd. had given large amounts of money free of interest to the assessee. In these circumstances it was held that the price charged by the appellant from Ponds India Ltd. could not be said to be the normal price of containers and, therefore, the action of the department in taking into account the notional interest on the advances given was upheld.

12.Metal Box case is clearly distinguishable. The amounts given as security deposit in the present cases represents only value of 21 days supply in a year whereas in Metal Box case large amounts of money had been advanced. Secondly, and what is more important, in Metal Box case the assessee had given fifty per cent discount to Ponds India Ltd. on its gross sale price and thereby charged lesser price than what was charged from the other buyers. In the present case the cigarettes are sold at the factory gate to the wholesale dealers at a uniform price irrespective of the fact whether the purchaser is buying the cigarettes on credit or against payment of money in cash.

13.Excise duty, as has been held, is on the manufacture of goods at the price paid. The price paid in the present case is the same by all the dealers. There is nothing to show that there was any special consideration which was shown to the dealers who had given the security deposit. Nor has it been shown by reference to any documents or data that because of the receipt of such deposit the price charged from all the buyers was reduced. Merely because interest pre-deposit was reduced from some dealers cannot, by itself, lead to the conclusion arrived at by the excise authorities and the Tribunal. This also followed from the decisions in the Indian Oxygen and Madras Rubber Factory's cases (supra). There was, thus, no justification for dis-regarding the uniform wholesale price which was being charged from all the dealers and adding the element of notional interest of the security deposit to the said price.

14.The additional Collector, in our opinion, was right in coming to the conclusion that Rule 5 of the Valuation Rules was not applicable in the present case as it was not shown that the price charged was not the sole consideration. When the appellants are not requiring all the dealers to give security deposit and it is only those who avail of credit facilities who are required to give the security deposit but get no discount or pay a reduced price, then in such a case excise duty can be charged only on the uniform price paid by the dealers without any addition of notional interest.

15.For the aforesaid reasons these appeals are allowed. The order of the CEGAT is set aside and extra demands raised by the respondent pursuant to the show cause notices issued by them are quashed. The appellants will also be entitled to costs.