

SUPREME COURT OF INDIA

Messrs C.T. Cotton Yarn Limited

Vs

Commissioner of Central Excise, Indore

Appeal (Civil) 6451-6452 of 2000

(Ashok Bhan and P. K. Balasubramanyan, JJ)

22.09.2006

JUDGMENT

P. K. BALASUBRAMANYAN, J.

1. The appellant challenges the decision of the Customs, Excise and Gold (Control) Appellate Tribunal, New Delhi in A.No.E/1715- 1716/97-D dated 19.07.2000. By the said order the Tribunal substantially dismissed the appeals filed by the appellant, but reduced the penalty imposed on the appellant by the Original Authority.

2. According to the appellant, it is a 100% export oriented unit engaged in the manufacture and export of cotton yarn. It purchases cotton from the domestic market for the manufacture of yarn. After the cotton is purchased it is subjected to carding and combing and only thereafter it is spun into yarn. According to the appellant, carding involves opening and separating out of fibres together with effective cleaning and combing is a process by which impurities and undesired short fibres are removed. During carding and combing, the fibre and noils can be separated and they are collected in one place by suction. This, according to the appellant, is a waste generated at the preparatory stage and it is cotton waste. It is impure cotton fibre.

3. Earlier, the appellant was paying duty on this cotton waste before clearing it and selling it in the Domestic Tariff Area. On finding that certain similar other manufactures were not paying duty on

the waste cotton thus generated and disposed of in the Domestic Tariff Area, the appellant sought clarification from the Collector of Central Excise and Customs, Indore taking up the position that cotton waste was not dutiable. On 9.9.1993, the appellant was informed that soft cotton waste arising out of indigenous material would not attract excise duty. The appellant started clearing and selling the waste cotton without payment of duty. On 16.09.1993, the Department wrote a letter to the appellant to explain under what circumstances the appellant was clearing the soft cotton waste and selling it in the Domestic Tariff Area without payment of duty. It is the case of the appellant that based on the clarification as above, it filed a fresh clarification list dated 17.9.1993 declaring soft cotton waste as non-excisable item and it continued clearing the same without payment of duty and selling it in the Domestic Tariff Area. On receipt of the communication dated 16.09.1993 from the Department, the appellant took up the position that soft cotton waste was not liable to duty since it was only cotton waste removed from the cotton domestically purchased so as to enable the appellant to make the yarn for the purpose of export.

4. On 16.3.1995, Finance Bill 1995 was introduced. In the First schedule to the Central Excise Tariff Act, 1985, a heading 52.02 was introduced covering cotton waste. The said Bill after having been passed, received the assent of the President of India on 26.5.1995 and thus became the Finance Act, 1995. On 4.12.1995 the Department issued a notice to the appellant to show cause why duty on the quantity of soft cotton waste cleared by the appellant and sold in the Domestic Tariff Area during the period from 1.5.1995 to 31.7.1995, be not imposed in terms of the proviso to Section 3(1) of the Act read with the concerned notification. Yet another notice was issued by the Department dated 22.7.1996 covering the period prior to the one covered by the earlier notice, the period from 16.3.1995 to 30.4.1995. The Department sought to invoke the extended period of limitation available under Section 11A of the Act. The appellant filed objections to the notices. In reply to the first notice it was put forward that soft cotton waste was not exigible to duty and that in any event, the demand for the period from 1.5.1995 to 3.6.1995 was barred by limitation, the demand having been made six months after the expiry of the said period. As regards the notice dated 22.7.1996, the appellant, in addition to the contention that no excise duty was leviable on soft cotton waste which it had disposed of in the Domestic Tariff Area, contended that the Department was not entitled to the extended period of limitation under the proviso to Section 11A of the Act since there was no suppression of any relevant fact on the part of the appellant and the Department was well aware all along that the appellant was removing soft cotton waste and disposing it of in the Domestic Tariff Area without paying duty.

5. On 5.5.1997, the Commissioner of Central Excise, Indore, rejected the contentions of the appellant. He confirmed the demand under the first notice, of Rs.15, 02, 211.18 towards duty. He also imposed a penalty of Rs.5 lakhs on the appellant. As regards the second notice, the Commissioner found that the Department was entitled to the benefit of the extended period under Section 11A of the Act and confirmed the demand under notice dated 22.7.1996 of Rs.7, 21, 739.63 and also imposed a fine of Rs.2.5 lakhs on the appellant.

6. The appellant filed appeals before the Appellate Tribunal. The appellate Tribunal imposed a condition that the appellant should deposit Rs.8 lakhs towards the duty and Rs.1 lakh towards the penalty before the appeals could be heard. According to the appellant the said sum was deposited on 31.10.1997. Before the Appellate Tribunal, the appellant contended that no manufacture was involved while soft cotton waste was being produced from the cotton that was being cleaned for the

purpose of making yarn for being exported and since there was no manufacture involved, no duty was leviable on soft cotton waste sold in the Domestic Tariff Area. It was also submitted that merely because the Finance Act has introduced an entry under Heading 52.02 in the first schedule to the Central Tariff Act covering cotton waste, it would not automatically mean that duty was leviable on the same. Any way, the amendment applied only to the period subsequent to the Finance Act 1995 and not before. It was also reiterated that the claim of the Department for extended period of limitation was unsustainable on the facts and in the circumstances of the case and that in any event the penalty imposed was unjustified. The Appellate Tribunal rejected the claim of the appellant mainly based on the admission of the representative of the appellant that after the 1995 Finance Act, soft cotton waste had become exigible to duty and further taking the view that since it has been specified in the first schedule to the Tariff Act as a dutiable item, the duty was payable at 50% of the rate of customs duty considering the fact that the appellant was 100% export oriented. It took the view that the Finance Act had come into force from the date of the Finance Bill. But the Tribunal, in the circumstances, reduced the penalty imposed by the Commissioner and reduced it to Rs.2.5 lakhs from of Rs.5 lakhs in respect of the period covered by the notice dated 4.12.1995 and to Rs.1.25 lakhs from Rs.2.5 lakhs in respect of the period covered by the notice dated 22.7.1996.

7. Learned counsel for the appellant submitted that soft cotton waste is not manufactured by the appellant but that it was only impure cotton separated from the cotton purchased from the domestic market for the manufacture of yarn intended solely for export. Counsel submitted that cotton waste thus generated itself and in the absence of any process of manufacture being involved, the mere fact that such cotton waste produced is sold regularly in the Domestic Tariff Area, would not make the same exigible to excise duty. He further contended that Heading 52.02 covering 'cotton waste' was introduced only by the Finance Act 1995 enacted on 26.5.1995 and it did not have effect from the date of introduction of the Finance Bill. He referred to Section 3, the charging section and emphasised that "it must be actually produced or manufactured before excise duty could be imposed". He also submitted that the Department was not entitled to have the benefit of the extended period of limitation and the demand covered by the notice dated 22.7.1996 was clearly barred and the demand covered by the notice dated 4.12.1995 was also barred insofar as it related to the claim for the period from 1.5.1995 to 3.6.1995. Counsel for the Department controverted these submissions and submitted that soft cotton waste was generated during the course of manufacture undertaken by the appellant when it manufactured yarn for export from cotton purchased from domestic market and this intermediate process cannot be separated and dealt with separately. He pointed out that in view of the declaration made in that behalf the amendment had been effective from the date of the Finance Bill. He also contended that manufacture was involved when soft cotton waste was produced and it was being regularly sold in the domestic market indicating that it was a marketable commodity and in the circumstances it was exigible to duty as rightly held by the Commissioner and the Appellate Tribunal. He also submitted that on the facts and in the circumstances of the case there was suppression of relevant material and information by the appellant and the Tribunal was justified in holding that the Department was entitled to the extended period of limitation available under Section 11A of the Act. Counsel, therefore, urged that no interference was called for with the decision of the Tribunal.

8. It is clear that the product involved herein is not a left over after the end product is manufactured. Here the cotton waste is generated during the process of manufacture of yarn. In other words, when cotton purchased in the domestic market is used for manufacture of yarn, by initiating the process of manufacture, at an intermediate stage, the so called cotton waste is produced, which is a marketable

commodity and which is regularly marketed. Therefore, one of the twin tests, namely, that the commodity which is produced is marketable and is regularly marketed as a product, is satisfied. It is by now established that merely because a commodity is included in the schedule, it will not be exigible to duty unless a process of manufacture is involved when that product emerges. Here, heading 52.02 has been brought in in the Schedule by the Finance Act, 1995. Though it is shown as an item bearing nil duty, since the appellant is a 100 per cent export oriented manufacturing entity it will be liable to duty as provided in the proviso to Section 3(1) of the Tariff Act. Therefore, the question involved is whether a process of manufacture is involved when the cotton waste is generated during the process of converting domestically purchased cotton into exportable yarn manufactured by the appellant.

9. In *State of Maharashtra vs. Pulgaon Cotton Mills Ltd.* [(7 SC)] This Court held that where a subsidiary product is turned out regularly and continuously in the course of manufacturing business and is also sold regularly from time to time, there may be attributed an intention to the manufacturer to manufacture and sell not merely the main item but also the subsidiary products. This Court relied on an earlier decision in *State of Gujarat vs. Raipur Manufacturing Company Limited* (SC)] in support of the position that manufacture was involved in that situation. Cotton waste generated was hence held to be by a process of manufacture. For the appellant it is submitted that the manufacture of a product may involve several processes and various changes in the raw material at different stages. Manufacture would occur at the point where the changes take the product to a point that commercially, it cannot be regarded as the original commodity, but, instead, recognised as a new distinct article. The decision of this Court in *J.G. Glass Industries* 5 is relied on in support.

10. The scope of the expanded definition of manufacture has been considered in the decision in *Shyam Oil Cake Ltd. Vs. Collector of Central Excise, Jaipur* 6 (SC)]. The appellate authority has essentially proceeded on the amendment to the schedule and inclusion of cotton waste therein and the admission of the representative of the appellant that subsequent to the inclusion in the schedule, cotton waste is taxable. It appears to us that the question whether cotton waste is dutiable as a manufactured product requires to be reconsidered by the Tribunal in the light of the various decisions of this Court brought to our notice and which may hereafter be brought to the notice of the Tribunal. The argument that it was only after the process of manufacture has started that the product has come into existence and it has marketability and hence, it is dutiable and the counter argument that it was only impure cotton which has got separated from the cotton purchased from the open market so as to enable the appellant to manufacture the yarn intended for export and this product produced at the intermediate stage still remains cotton and it is not a manufactured product, have both to be considered in the light of the decided cases. In this situation, we think it appropriate to set aside the order of the Tribunal and remand the appeals filed by the appellant to the Tribunal for a fresh decision. We think that this aspect needs to be reconsidered by the Tribunal afresh and a fresh decision taken. We, therefore, set aside the order of the Tribunal on this aspect and direct the Tribunal to decide the appeals afresh based on the finding to be rendered on this question. All contentions including whether the department could invoke the extended period of limitation are left open.

11. Thus, the appeals are allowed in part, the orders of the Tribunal are set aside and the appeals filed by the appellant before the Tribunal are remanded for a decision afresh on the question referred to above. The parties are directed to bear their respective costs.

