

SUPREME COURT OF INDIA

Commissioner of Central Excise, Delhi

Vs.

Frick India Ltd

C.A.Nos.1825-1827 of 2002

(S. H. Kapadia and B. Sudershan Reddy, JJ.)

21.09.2007

JUDGEMENT

KAPADIA, J.:-

1. These civil appeals are filed by the Department under Section 35-L(b) of the Central Excise Act, 1944 against order passed by CEGAT dated 18.9.2001 in Final Order No.354-356/2000-A, in Appeal Nos.E/1151 and 1192/2000-A, E/3402/ 2000-A whereby the Tribunal allowed the appeals filed by the assessee (respondents).

2. Assessee-M/s. Frick India Ltd., Faridabad, (M/s. FIL) manufactures air-con ditioning and refrigerating machinery and appliances classifiable under Chapter 84 of the Central Excise Tariff Act, 1985.

3. Assessee cleared compressors falling under tariff sub-heading 8414.10. They also cleared to its

buyers separately "fly wheel" under separate tariff sub-heading 8483.00, "safety valve" under separate tariff sub heading 8481.80 and "filter" under separate tariff sub-heading 8421.00. Apart from the above three items, assessee supplied to its buyers bought-out items, namely, V. belt, motor, pulley, belt guard, gauge, gauge board, angle valve, M.S. male flange, C.A.F. Gasket, set of tools, bolts and nuts, etc.

4. On 4.9.98, show cause notice was given to M/s. FIL in which it was alleged by the Department that the assessee had evaded payment of duty on the full value of the compressors, manufactured and cleared by them, by separately invoicing clearance of bought-out items and manufactured items. At this stage, it may be noticed that the factory of the assessee is in Faridabad where the items, manufactured and cleared, consisted of compressor, fly wheel, safety valve and filter ("manufactured items", for short) whereas from their trading office in New Delhi, the bought-out items consisted of V. belt, pulley, belt guard, angle valves and other items referred to in para 3 of the show cause notice ("bought-out items", for short). According to the show cause notice, assessee had knowingly cleared manufactured items and bought-out items separately; that the value of the bought-out items and manufactured items like fly wheel, safety valve and filter were includible in the assessable value of the compressor as without the said items the compressor was non-functional; that, M/s. FIL had deliberately undervalued the compressor and overvalued the accessories/ parts which were supplied separately to the buyers; that, there was a difference between the cost price and the declared assessable value for compressor and in the circumstances the assessee became liable to pay differential duty amounting to Rs.4,46,19,392.65 on the accessories which stood worked out on the basis of includibility of the value of bought-out items + duty on the parts of accessories, manufactured and cleared by the assessee, at lower rate of duty during the period August 1993 to March 1998. According to the Department, the said accessories were in effect parts of the compressor as the compressor was non-functional without the said items.

5. In reply to the show cause notice, assessee pleaded that when the manufactured items, namely, fly wheel, safety valve and filter were supplied along with the compressors, the said items were classifiable under their own respective Headings, namely, 84.83 (fly wheel), 84.81 (safety wheel) and 84.21 (filter). According to the assessee, the said three items were not classifiable as "compressor" under tariff Heading 84.14. In this connection, reliance was placed by the assessee on Note 2 to Section XVI of the Central Excise Tariff Act, 1985 which, inter alia, states that parts of machines are to be classified under their respective headings.

6. By order dated 31.12.99, the Commissioner held that fly wheel, safety valve and filter were essential parts in the compressors; that, similarly bought-out items, namely, motor pulley, V. belt, belt guard, angle valve etc. were also to be treated as parts, as the compressor was non-functional without such bought-out items; that the compressors supplied at sites by the assessee were basically compressors in SKD condition; in that connection reliance was placed on General Interpretative Rule 2(a), Part-V Section XVI of HSN, Part-III Section XVI of the Interpretative Notes 2(a) and 3(b) as also Note 3 to the Central Excise Tariff Act, 1985; that from the cost statements filed by the assessee, the difference between the manufacturing cost and the declared assessable value for compressors of different sizes was clear. Therefore, in the aforesaid circumstances, the show cause

notice stood confirmed.

7. Aggrieved by the decision dated 31.12.99 given by the Commissioner, the assessee carried the matter in appeal to CEGAT which took the view that the compressor, cleared by the assessee, stood cleared as a "stand-alone" item and that it was not removed in an unassembled or disassembled condition and, therefore, there was no question of applying General Interpretative Rule 2(a), Part-V Section XVI of HSN; that, similarly Part-III of Section XVI of Interpretative Notes of HSN was not applicable as the compressor was cleared as a "stand-alone" item. According to the Tribunal, since parts of the compressor, namely, fly wheel, safety valve and filter as also bought-out items were classifiable under separate headings, namely, 84.83, 84.81 and 84.21, the Department had erred in classifying them as "compressors". According to CEGAT, the said items were classifiable under specific headings by virtue of Note 2(a) to Section XVI of the Central Excise Tariff Act, 1985 and, therefore, the said three items could not have been classified as "compressor". However, on the question as to whether the assessee had transferred the value of the compressor to the value of the parts, the matter was remitted to the Commissioner. The Department had alleged in the show cause notice that the assessee had undervalued the compressors and had overvalued the accessories which were supplied either in the same packing or separately to the buyers. This question has been remitted to the Commissioner. Aggrieved by the decision delivered by the Tribunal dated 18.9.01, the Department has come to this Court by way of the present civil appeals.

8. We quote hereinbelow Rule 2(a) of the Rules for Interpretation of the Schedule to the Central Excise Tariff Act, 1985 which reads as below :

"2 (a) Any reference in a heading to goods shall be taken to include a reference to those goods incomplete or unfinished, provided that, the incomplete or unfinished goods have the essential character of the complete or finished goods. It shall also be taken to include a reference to those goods complete or finished (or falling to be classified as complete or finished by virtue of this rule), removed unassembled or disassembled."

9. We also quote hereinbelow Section Note 2 to Section XVI of the Central Excise Tariff Act which reads as below :

"2. Subject to Note 1 to this Section, Note 1 to Chapter 84 and to Note 1 to Chapter 85, parts of machines (not being parts of the articles of heading 84.84, 85.44, 85.45, 85.46 or 85.47) are to be classified according to the following rules :

(a) Parts which are goods included in any of the headings of Chapter 84 or Chapter 85 (other than heading Nos. 84.09, 84.31, 84.48, 84.66, 84.73, 84.85, 85.03, 85.22, 85.29, 85.38 and 85.48) are in

all cases to be classified in their respective headings;

(b) Other parts, if suitable for use solely or principally with a particular kind of machine, or with a number of machines of the same heading (including a machine of heading No. 84.79 or heading No.85.43) are to be classified with the machines of that kind or in heading 84.09, 84.31, 84.48, 84.66, 84.73, 85.03, 85.22, 85.29 or 85.38 as appropriate. However, parts which are equally suitable for use principally with the goods of heading Nos. 85.17 and 85.25 to 85.28 are to be classified in heading No. 85.17;

(c) All other parts are to be classified in heading 84.09, 84.31, 84.48, 84.66, 84.73, 85.03, 85.22, 85.29 or 85.38 as appropriate or, failing that, in heading No. 84.85 or 85.48."

10. We also quote hereinbelow Section Note 2 to Section XVI of the HSN which reads as below :

"2. Subject to Note 1 to this Section, Note 1 to Chapter 84 and Note 1 to Chapter 85, parts of machines (not being parts of the articles of heading 84.84, 85.44, 85.45, 85.46 or 85.47) are to be classified according to the following rules :

(a) Parts which are goods included in any of the headings of Chapter 84 or 85 (other than headings 84.09, 84.31, 84.48, 84.66, 84.73, 84.85, 85.03, 85.22, 85.29, 85.38 and 85.48) are in all cases to be classified in their respective headings;

(b) Other parts, if suitable for use solely or principally with a particular kind of machine, or with a number of machines of the same heading (including a machine of heading 84.79 or 85.43) are to be classified with the machines of that kind or in heading 84.09, 84.31, 84.48, 84.66, 84.73, 85.03, 85.22, 85.29 or 85.38 as appropriate. However, parts which are equally suitable for use principally with the goods of headings 85.17 and 85.25 to 85.28 are to be classified in heading 85.17;

(c) All other parts are to be classified in heading 84.09, 84.31, 84.48, 84.66, 84.73, 85.03, 85.22, 85.29 or 85.38 as appropriate or, failing that, in heading 84.85 or 85.48."

11. We quote hereinbelow Explanatory Note dealing with Parts of a Machine in HSN which reads as below :

"PARTS

In general, parts which are suitable for use solely or principally with particular machines or apparatus (including those of heading 84.79 or heading 85.43), or with a group of machines or apparatus falling in the same heading, are classified in the same heading as those machines or apparatus subject, of course, to the exclusions mentioned in Part (I) above. Separate headings are, however, provided for :

(A) Parts of the engines of heading 84.07 or 84.08 (heading 84.09).

(B) Parts of the machinery of headings 84.25 to 84.30 (heading 84.31).

(C) Parts of the textile machines of headings 84.44 to 84.47 (heading 84.48)

(D) Parts of the machine-tools of headings 84.56 to 84.65 (heading 84.66).

(E) Parts of the office machines of headings 84.69 to 84.72 (heading 84.73).

(F) Parts of the machines of heading 85.01 or 85.02 (heading 85.03).

(G) Parts of apparatus of headings 85.19 to 85.21 (heading 85.22).

(H) Parts of apparatus of headings 85.25 to 85.28 (heading 85.29).

(I) Parts of apparatus of heading 85.35, 85.36 or 85.37 (heading 85.38).

The above rules do not apply to parts which in themselves constitute an article covered by a heading of this Section (other than headings 84.85 and 85.48); these are in all cases classified in their own appropriate heading even if specially designed to work as part of a specific machine. This applies in particular to :

(1) Pumps and compressors (headings 84.13 and 84.14)

(2) Filtering machinery and apparatus of heading 84.21.

(3) Lifting and handling machinery (heading 84.25, 84.26 or 84.28).

(4) Taps, cocks, valves, etc. (heading 84.81).

(5) Balls or roller bearings, and polished steel balls of a tolerance not exceeding 1% or 0.05 mm, whichever is less (heading 84.82).

(6) Transmission shafts, cranks, bearing housings, plain shaft bearings, gears and gearing (including friction gears and gear boxes and other speed changers), flywheels, pulleys and pulley blocks, clutches and shaft couplings (heading 84.83).

(7) Gaskets and similar joints of heading 84.84."

12. We quote hereinbelow Part V Section XVI of HSN which reads as below :

"(V) UNASSEMBLED MACHINES

(See General Interpretative Rule 2 (a))

For convenience of transport many machines and apparatus are transported in an unassembled state. Although in effect the goods are then a collection of parts, they are classified as being the machine in question and not in any separate heading for part. The same applies to an incomplete machine having the features of the complete machine (see part IV), presented unassembled (see also in this connection the General Explanatory Notes to Chapters 84 and 85). However, unassembled components in excess of the number required for a complete machine or for an incomplete machine

having the characteristics of a complete machine, are classified in their own appropriate heading."

13. We quote hereinbelow Part III Section XVI of the Interpretative Notes of HSN which reads as below :

"(III) ACCESSORY APPARATUS

(See General interpretative Rules 2(a) and 3(b) and Section Notes 3 and 4)

Accessory instruments and apparatus (e.g., manometers, thermometers, level gauges or other measuring or checking instruments, output counters, clockwork switches, control panels, automatic regulators) presented with the machine or apparatus with which they normally belong are classified with that machine or apparatus, if they are designed to measure, check, control or regulate one specific machine or apparatus (which may be a combination of machines (see Part VI) or a functional unit (see part VII)). However, accessory instruments and apparatus designed to measure, check, control or regulate several machines (whether or not of the same type) fall in their own appropriate heading."

14. Chargeability from excise duty is on the manufacture of excisable goods. The assessee has to pay duty on the manufacture of such goods. With chargeability, question of quantification of duty comes in. Classification decides the applicable rate. It is followed by valuation i.e. value on which the rate is to be applied. The concept of "classification" is, therefore, different from the concept of "valuation". In the present matter there is confusion in application of the aforesaid two concepts by the Commissioner. In our view, the thrust of the show cause notice is towards undervaluation and not classification. This is made clear even in the order of the Commissioner vide para 53 which reads as under :

"53. On consideration of the arguments of both sides and the facts on record I find that show cause notice dated 1.10.86 proposed classification of flywheel, safety valve and filter under SH 8414.91 of CET 1985. The Show Cause Notice dated 10.11.86, which superseded the above SCN also proposed the same classification. The present show cause notice also does not propose any fresh classification. Here the issue involved is different. The issue is not whether the items like fly wheel, pulley and safety valve are classifiable under SH 8414.10 or 8414.19 or in the specific sub-heading where these items have been specifically mentioned. The issue here is whether M/s. FIL have made correct assessment of duty and have paid appropriate duty leviable thereon on the compressors cleared by them during the period relevant to this Show Cause. The case of the Department is that since these items are essential parts of the compressors and have been supplied along with compressors in SKD condition, the value of such parts is includible in the assessable value of compressors. I have already come to the conclusion that the above items are essential parts of the compressors as discussed in paragraphs 42 to 48 supra. Thus the point raised by the notice becomes

redundant."

(Emphasis supplied by us)

15. As rightly observed by the Tribunal, the General Interpretative Rule 2(a) has no application to the present case for two reasons. Firstly, the compressor manufactured by the assessee was removed as a "stand alone" item. It was not cleared in an unassembled or disassembled condition. Secondly, section and chapter notes in Central Excise Tariff Act, 1985 and the Interpretative Rules do not provide guidelines for valuation of excisable goods as they decide classification of a product under different headings/sub-headings of the tariff. Lastly, under Note 2(a) to Section XVI of the Central Excise Tariff Act, 1985 as well as Note 2(a) to Section XVI of HSN read with Explanatory Note referable to Parts of a Machine in HSN clarifies that payment of duty at the appropriate rates, relevant to the respective headings alone, shall apply. In the present case, as stated above a complete compressor stood cleared under tariff Heading 84.14. Duty has been paid thereof. Similarly, safety valves were cleared by the assessee on payment of duty under tariff Heading 84.81. Lastly, filters were also cleared by payment of duty under tariff Heading 84.21. In the circumstances, on the question of classification the Tribunal was right in holding that parts/accessories could not have been classified as "compressors" under tariff Heading 84.14.

16. However, we find merit in these civil appeals filed by the Department on the question of valuation. As stated above, the concept of "classification" is different from the concept of "valuation". In the present matter, along with the "stand-alone" compressor, the assessee has supplied fly wheel, safety valve and filter to its buyers. They have also supplied bought-out items like V belt, motor, pulley, belt guard, gauge, gauge board, angle valve, M.S. male flange, C.A.F. Gasket, set of tools, bolts and nuts, etc. to their buyers, as a package. Therefore, on the question of valuation, the Commissioner should have examined the pricing aspect of the entire package supplied by the assessee to its buyers. For example, when a ceiling fan is sold to the buyer, apart from the parts of the ceiling fan, there may be a remote which is a part of the package supplied to the buyer. That remote is fan-specific in matter of valuation since the remote is an additional feature provided with the ceiling fan its value has also to be taken into account. This is because the remote which operates the fan may be an accessory but still it makes value addition and, therefore, its value is liable to be included in the assessable value of the ceiling fan. These aspects have not been considered by the Commissioner, therefore, in addition to the question remitted by CEGAT to the Commissioner we also direct the Commissioner to de novo consider the question of valuation. In this connection, the Commissioner will call for the cost statements and shall also ascertain the manner in which the assessee has priced its goods. The Commissioner may also consider invocation of Section 14A of the Central Excise Act, 1944 which deals with "special audits in certain cases". In our view, in the present matter "costing" as a concept will play an important role and, therefore, if the Commissioner so deems fit he can order special audits and call for the report of the cost accountant to assist him (Commissioner) to arrive at the correct value of the entire package cleared by the assessee from its factory gate.

17. Accordingly, the civil appeals filed by the Department are partly allowed with no order as to costs.

Appeal partly allowed.