BOMBAY HIGH COURT

Union of India

Vs

Hindustan Spinning

(B Srikrishna and S Bharucha , JJ.)

21.08.1990

JUDGMENT

Srikrishna, J.

1. The appeal is directed against the order which has been delivered by Pendse, J. making the rule granted in writ petition absolute in terms of prayer (a). Pendse, J. followed the judgment of Pratap J. in O.O.C.J. Miscellaneous Petition No. 215 of 1978 in Shreeram Mills Limited and Another v. Union of India and Others delivered on 15th of June 1982. Pratap, J. in turn followed the judgment of the Division Bench of the Gujarat High Court in Aryodaya Spinning and Weaving Company Limited v. Union of India and Others - 1981 (8) E.L.T. 274.

2. The facts which are material for resolving the controversy in appeal may be summarised as under : The First Respondent is a composite textile mills which manufactures yarn and cotton textile fabrics. In its manufacturing process the first respondent uses both cellulosic spun yarn as well as cotton yarn. Cellulosic spun yarn, cotton yarn and cotton fabrics which are ultimately manufactured by the first respondent are all excisable commodities.

3. Cellulosic spun yarn is liable to excise duty under Tariff Item No. 18, cotton yarn is liable to excise duty under Tariff Item No. 18A and cotton fabrics are liable to excise duty under Tariff Item No. 19 in the Schedule to the Central Excises and Salt Act, 1944 (hereinafter referred to as "the Act"). Under Sections 6, 12 and 37 of the Act power has been conferred upon the Central Government to make rules and one of such powers is the power to make rules for exempting goods from excise duty in special cases. In exercise of this rule making power the Central Government has made Central Excise Rules, 1944. Rule 8 of these Rules deals with the power to authorise exemption from duty in special cases. Under this Rule -

"The Central Government may, from time to time, by notification in the Official Gazette, exempt, (subject to such conditions as may be specified in the notification) any excisable goods

from the whole or any part of duty leviable on such goods."In exercise of this power under Rule 8 the Central Government had issued Notification No. 131 of 1977 dated June 18, 1977 granting partial exemption to cotton yarn falling under Tariff Item No. 18A from payment of excise duty. Composite mills were, however, excluded from the operation of the the said notification by virtue of clause (vii) of the proviso to this notification. By another Notification No. 132 of 1977, issued on the same day, i.e., on June 18, 1977, cellulosic spun yarn falling under Tariff Item No. 18II(i) and cotton yarn falling under Tariff Item No. 18A(i) were exempted wholly from excise duty leviable thereon when these yarns were used for weaving of cotton fabrics in the composite mills. A third notification was also issued on June 18, 1977, i.e., Notification No. 135 of 1977. Under this notification partial exemption to cotton fabrics falling under Tariff Item No. 19(i) of the First Schedule of the Act was granted. As a result of these notifications, particularly Notification No. 132 of 1977, duty on cellulosic spun yarn and cotton yarn was wholly exempt and duty on cotton fabrics falling under Tariff Item No. 18A (sic) was partially exempt to the extent mentioned in the Notification No. 135 of 1977.

4. On July 15, 1977, in exercise of the same power under Rule 8, the Central Government issued three notifications namely Notification Nos. 224, 225 and 226 of 1977. By Notification No. 224 of 1977 Clause (vii) of the proviso and explanation (ii) of Notification No. 131 of 1977 were omitted. By Notification No. 225 of 1977 Notification No. 132 of 1977 was rescinded and by Notification No. 226 of 1977 the earlier Notification No. 135 of 1977 was superseded and the new rates of partial exemption in the case of cotton fabrics were prescribed.

5. As a result of these three notifications issued on July 15, 1977, the complete exemption which was granted in respect of cellulosic spun yarn and cotton yarn used by composite mills manufacturing cotton fabrics was taken away. On account of the deletion of Clause (vii) of the proviso to Notification No. 131 of 1977, excise duty on cellulosic spun yarn and cotton yarn even when used by composite mills in manufacturing cotton fabrics, could be levied at the rates mentioned in the Notification No. 131 of 1977 and in respect of cotton fabrics, by virtue of Notification No. 226 of 1977, a different table was prescribed for levying excise duty on cotton fabrics. The result of these three notifications was to put forward a substantially different scheme for levying excise duty on cellulosic spun yarn and cotton yarn of all kinds used by all types of manufacturers. In the case of composite mills however, the exemption which was available from June 18, 1977 in respect of cellulosic spun yarn and cotton yarn used in manufacturing of cotton fabrics was taken away. No difficulty appears to have arisen in prospective operation of the Notifications of July 15, 1977. However, as regards cotton fabrics which were manufactured by composite mills after June 18, 1977 from cellulosic spun yarn and cotton yarn and which were still lying in stock and not cleared, a special provision was made in the second proviso in the

Notification dated July 15, 1977, i.e. No. 226 of 1977. That proviso is subject matter of controversy. The relevant proviso reads as under -

> "Provided further that in cases where cotton fabrics have been produced in a composite mill or are produced therein and in the production of such cotton fabrics cellulosic spun yarn falling under sub-item III(i) of Item No. 18 of the said First Schedule or cotton yarn falling under Item No. 18A(i) of the said First Schedule, or both, on which no duty of excise was paid prior to the 15th day of July, 1977, was or is used, the duty payable on such fabrics shall be -
>
> (a) at the appropriate rate of duty as specified in this notification plus,
>
> (b) the duty payable on such cellulosic spun yarn or cotton yarn or both, as the case may be under the notification of the Government of India in the Department of Revenue and Banking No. 131/77-Central Excise, dated the 18th June, 1977."

6. The first respondent was served with a show-cause-cum-demand notice dated 19th May, 1979 issued by the Assistant Collector, Central Excise, Bombay 'E' Division. The purport of the said notice was that the first respondent had removed cotton yarn weighing 2,58,103 Kgs. which was excisable under T.I. No. 18A(i) as detailed in Annexure to the said show cause notice "held in stock in their various Departments as on the mid-night of 14th/15th July, 1977 and used the same for fabrication of cotton fabrics falling under T.I. No. 19-I" without payment of central excise duty leviable thereon amounting to Rs. 2,19,618.90 Ps. in terms of Notification No. 137 of 1977 as amended by the Notification No. 226 of 1977 dated 15th July, 1977, read with the relevant rules and the provisions of the Act. Annexed to the show-cause-cum-demand notice was a detailed statement showing yarns of different kinds which were alleged to have been lying in the various Departments as on the relevant date. The Departments specified in the annexure to the show cause-cum-demand notice are - Winding, Warping, Sizing, Weaving, Weft, Reeling and Packing.

7. The petitioners challenged the show-cause-cum-demand notice issued to them by their writ petition. They contended that the cellulosic spun yarn and cotton yarn which had already been manufactured prior to the mid-night of 14th/15th July had earned exemption in terms of the notification which was operative prior to 15th July, 1977 and it was not permissible for the Central Government purporting to exercise powers under Rule 8, retrospectively to take away the exemption which was already operating in respect of such yarn. They, therefore, contended that clause (b) to the first proviso to clause (viii) amounted to giving restrospective effect to the duty leviable under the Notification No. 226 of 1977 dated 15th July, 1977 and that the Central

Government had no power under the Rules retrospectively to take away the exemption which had already been earned by the cellulosic spun yarn and cotton yarn manufactured between 18th June, 1977 to 14th July, 1977. By the time the writ petition came up for hearing, there was already a judgment of a Single Judge, Pratap, J., dated June 15, 1982, in O.O.C.J. Miscellaneous Petition No. 215 of 1978 which held the field. Pendse, J. by his judgment dated July 10, 1986 followed the judgment of Pratap, J. in O.O.C.J. Miscellaneous Petition No. 215 of 1978 and made the rule absolute in terms of prayer (a) quashing and setting aside the show-cause-cum-demand notice dated 19th May, 1979 issued to the first respondent. The appellants are in appeal against the said decision of Pendse, J.

8. Mr. Sethna, the learned counsel for the appellants, basically raised three contentions. He strenuously urged that the judgment under appeal and the judgment of Pratap, J. in O.O.C.J. Miscellaneous Petition No. 215 of 1978 were inconsistent with the law laid down by the Supreme Court in *Wallace Flour Mills Company Ltd. v. Collector of Central Excise*[1] - and hence must be held to have been overruled. He further contended that the yarn in question could not be said to have earned exemption inasmuch as it had not been used in the manufacture of cotton fabrics as on the mid-night of 14th/15th July, 1977 and therefore it had not at all earned the exemption in terms of the Notification No. 132 of 1977, dated 18th June, 1977. He also contended that even assuming that the yarn in question could be said to have been removed and could be said to have earned exemption, the requisite procedure for such removal as prescribed under the Rules had not been followed and therefore it could not be deemed to be removal within the meaning of Rule 9.

9. We shall first take up the second contention of Mr. Sethna for consideration. In support of his submission, Mr. Sethna relied on the judgment of the Supreme Court in *State of Uttar Pradesh v. Ramagya Sharma Vaidya* - . The Supreme Court in this case was concerned with interpreting the word "use" as used in the Iron and Steel (Control) Order, 1956. In the context of the said provision of law the Supreme Court took the view that the word "use" suggests something done positively, namely, utilisation or disposal of the stock of iron and mere non-user could not be said to have been included in the word "use" so as to incur the penalty prescribed under the said order. We think that this Supreme Court judgment is of no assistance to the appellants since it arose out of the peculiar provisions of the Iron and Steel (Control) Order referred to in the judgment. Mr. Sethna also relied on the decision of the Gujarat High Court in the case of Commissioner of Income-tax, Gujarat v. Suhrid Geigy Ltd. - Vol. 133 (1982) ITR 884 in support of his contention. In this case the Court was concerned with the provisions of Section 32 of the Income Tax Act and Rule 5 thereunder which dealt with the point of time when the assessee became entitled to claim depreciation in respect of the assets used in his profession or business. The Court, after

considering the provisions of the Act, took the view that the mere fact that the asset is installed, and the further fact that the installed asset by process of aging suffers depreciation of value, would not entitle the assessee to claim depreciation under Section 32(1) of the Income Tax Act since the allowance thereunder was not claimable in respect of the natural wear and tear by reason of the aging process, but was relatable to the user of the assets in the business of the assessee. Here again in the judgment does not carry us any further and we do not think that it advances the contention of Mr. Sethna. As far as the facts of the present case are concerned, the short answer to Mr. Sethna's second contention is found in the wording of the show-cause-cum-demand notice itself. It was the case of the appellants in the said notice that cotton yarn of specified quantity which was held in stock in their various Departments as on the mid-night of 14th/15th July, 1977 had been removed and used for fabrication of cotton fabrics. In the face of this case made out in the show-cause-cum-demand notice, we are not in a position to accept the contention of Mr. Sethna that the yarn in question had not been "used" and therefore it had not earned the exemption under the notification which held the field prior to 15th July, 1977. Apart from this fact, it is also necessary to emphasise that in the annexure to the show-cause-cum-demand notice the appellants had specified the various Departments in which the yarn was held in stock. Considering the fact that yarn in question was manufactured in the Spinning Department, the fact that the stock thereof was held in other Departments would be indicative of the commencement of the process of use so as to earn exemption within the meaning of the Notification No. 132 of 1977. We do not read the expression "use" as contained in the Notification No. 132 of 1977 and as implying only the terminal stage, viz. the cotton fabric rolling out of the machine. In our view, upon a rational construction of the said expression "use" occurring in Notification No. 132 of 1977, when the yarn in question is taken out of the Department where it was manufactured with the specific intent of being consumed in the process of further manufacture of the cotton fabrics, the process of use can be said to have begun and the yarn in question could be said to have satisfied the condition of "use" as prescribed in the Notification No. 132 of 1977 so as to become eligible for the exemption which was available between 18th June, 1977 to 14th July 1977. Mr. Sethna also made an attempt to sustain this contention by reference to the judgment of the Division Bench of the Gujarat High Court in Aryodaya Spg. and Wvg. Co. Ltd. v. Union of India and Others - 1981 (8) E.L.T. 274. In our view, a careful reading of this judgment does not support the second contention of Mr. Sethna. We, therefore, reject the second contention of the appellants that the yarn in question had not been used in the manufacture of cotton fabrics.

10. Turning now to the first contention of Mr. Sethna, though, at first blush, it appears to be formidable in view of the apparent support of observations of the Supreme Court in Wallace Flour Mills case (supra), a closer examination shows the contention to be without substance. In

the Wallace Flour Mills case the company had pre-budget stocks of goods of various food products which were not leviable to duty till 28th February, 1987. The goods became dutiable by the Finance Bill, 1987-88 with effect from 1st March, 1987. The question, therefore, which fell for consideration before the Supreme Court was whether the goods which had been manufactured prior to 1st March, 1987, when they were completely exempted from excise duty, could be made dutiable by attracting duty on 1st of March, 1987. In other words, the question was what was the point of time at which the manufactured goods became subject to excise duty. The Supreme Court answered this question by taking the view that even though the taxable event is the manufacture or production of the excisable articles, the duty can be levied and collected at a later stage for administrative convenience and the scheme of the Act and the relevant Rules framed under the Act, particularly Rule 9A, revealed that though the taxable event is the fact of manufacture or production of excisable articles, the payment of duty is related to the date of removal of such articles from the factory. The Supreme Court observed, -

> "..... Excise is a duty on manufacture or production. But the realisation of the duty may be postponed for administrative convenience to the date of removal of goods from the factory. Rule 9A of the said rules merely does that. That is the scheme of the Act. It does not, in our opinion, make removal be the taxable event. The taxable event is the manufacture. But the liability to pay the duty is postponed till the time of removal under Rule 9A of the said Rules ..... On the basis of Rule 9A of the said rules, the Central Excise authorities were within the competence to apply the rate prevailing on the date of removal. We are of the opinion that even though the taxable event is the manufacture or the production of an excisable article, the duty can be levied and collected at a later date for administrative convenience."

Mr. Sethna places strong reliance on this judgment and contends that on the date on which the cotton fabrics were "removed" they were liable to duty in accordance with Notification No. 226 of 1977 dated 15th July, 1977 and, therefore, irrespective of when the cotton yarn had been manufactured, the duty was payable thereupon in terms of Notification No. 226 of 1977 which was in operation on the date of removal. Relying on the Supreme Court judgment in Wallace Flour Mills case, he contends that the levy of duty becomes operative both as to the levy and the rate, as on the date of removal and, therefore, the judgment of Pratap, J. taking the view that clause (b) of the first proviso to clause (viii) of the Notification No. 226 of 1977 amounts to retrospective levy of excise duty on the exempt yarn manufactured between 18th June, 1977 and 14th July, 1977, is erroneous. In his submission, the duty was levied prospectively from the point of time when the Notification No. 226 of 1977 became operative, i.e. the mid-night of 14th/15th of July, 1977 and merely because in the newly introduced scheme the duty includes certain duty

calculated with reference to the duty which had not been imposed on the cotton yarn between 18th June, 1977 to 14th July, 1977, for the purpose of calculation, it cannot be assumed that such imposition amounts to retrospective levy of excise duty on the yarn in question.

11. Mr. Shah, the learned counsel for the first respondent, countered the submission on this aspect of the matter by placing reliance on the judgment of the Division Bench of this Court, to which one of us (Bharucha, J.) was a party, given in the case of *The Union of India and Others v. The Shreenivas Cotton Mills Ltd. - (*Appeal No. 250 of 1980 decided on 4th December, 1986). In this case, the question arose as to at which exact point of time excisable articles intended for consumption or utilisation could be said to have been removed. This was also a case of a composite textile mill which had consumed the yarn manufactured by it for the purpose of manufacturing cotton textile fabrics. The contention that was urged on behalf of the Department in the Shreenivas Cotton Mills case was also somewhat similar. The Department had urged that the levy of the excise duty had not become crystallised on the date of manufacture of the yarn and hence the respondents were obliged to make payment at the rates current on the date of clearance of the fabric made out of the yarn. The Division Bench placed reliance on the explanation of Rule 9, which was brought into effect retrospectively from 2-10-1944, and a similar statement annexed to the show-cause notice therein which was issued to the company in the said case. There also the Department had alleged that the yarn in question was lying in various Departments, such as the Weaving Shed, and from the said description the Division Bench took the view that the yarn in question was in the process of blending and, therefore, in the process of manufacture. Even assuming that it was still yarn, it had been removed from the Department in which it had been made and transported to the weaving shed and other Departments for manufacture of cloth, and, therefore, the process of consumption and utilisation must be held to have commenced. In this view of the matter, the Division Bench dismissed the appeal of the Department and upheld the judgment of the single Judge.

12. Since the single Judge in the decision appealed against has heavily relied on the decision of the Gujarat High Court in the Aryodaya's case cited (supra) and since in the present appeal Mr. Sethna, the learned counsel for the Appellants, has argued at length to show that the judgment in Aryodaya Spinning Company's case is not good law in view of the subsequent judgment of the Supreme Court in Wallace Flour Mills case, it is necessary to deal with the case of Aryodaya Spinning Company at greater length.

13. So far as the facts of Aryodaya case are concerned, they are set out in paragraphs 1, 2 and 3 of the judgment and are substantially similar to the facts of the case before us. In this case also the petitioners had challenged clause (b) of the proviso to clause (viii) of Rule 8 and contended that it was violative of Article 14 of the Constitution of India as well as ultra vires the powers of

the Government under the Act, on the ground that the rule enabled the authorities to retrospectively levy excise duty on yarn which had been wholly exempted from duty during the relevant period though there was no such power to levy retrospective duty granted to the rule making authority. The reasoning of the Division Bench is contained in paragraph 17 of the judgment. The Gujarat High Court took the view that it was not open to the Central Government to provide for levy of excise duty on cellulosic spun yarn or cotton yarn which had been used in making cotton fabrics manufactured prior to July 15, 1977, by a composite mill, since under the notifications then in force, such yarn was wholly exempted from payment of excise duty when the yarn was wholly exempted from payment of excise duty when the yarn was used for manufacture of cotton fabrics in a composite mill. The Division Bench observed in paragraph 17, "The taxable event in the light of which excise duty on cellulosic spun yarn or cotton yarn was payable was over before July 16, 1977. The event which had earned exemption for cellulosic spun yarn and cotton yarn had also occurred, namely, use of such cellulosic spun yarn and cotton yarn by a composite mill for the manufacture of cotton fabrics. What Clause (b) of the impugned second proviso to Notification No. 226 of 1977 was seeking to do was to collect at the stage of removal from the premises in question the excise duty, not on cotton fabrics, but on cotton yarn and cellulosic spun yarn."We must point out here that the judgment in the Aryodaya Spinning Company's case was given by the Division Bench of the Gujarat High Court on 10th September, 1980, at which time Rule 9 did not contain the explanation. The explanation was added by the amending notification dated 28th February, 1982, although with retrospective effect from 28th February, 1944. The Gujarat High Court, while deciding the Aryodaya Spinning Company's case did not therefore have the benefit of the explanation.

14. The newly added explanation reads as under -

"Explanation. - For the purposes of this rule, excisable goods produced, cured or manufactured in any place and consumed or utilised -

(i) as such or after subjection to any process or processes; or

(ii) for the manufacture of any other commodity, whether in a continuous process or otherwise, in such place or any premises appurtenant thereto, specified by the Collector under sub-rule (1), shall be deemed to have been removed from such place or premises immediately before such consumption or utilisation."The explanation has been added to take care of the situation where an employer produces excisable goods and consumes or utilises them for the manufacture of any other commodity. The effect of the explanation is that the intermediate product is deemed to have been removed from the place or premises appurtenant thereto, specified by the Collector under sub-rule (1), immediately before such consumption or utilisation. In other words, by a legal

fiction, such intermediate product is deemed to have been removed immediately before its consumption or utilisation.

15. This Explanation was relied upon by the Division Bench of our High Court in Shreenivas Cotton Mills case (supra) to come to the conclusion that the levy of excise would be attracted when the intermediate product, i.e. yarn, had been manufactured and transported to other Departments for the purpose of manufacture of cloth. Reading the Aryodaya Spinning Company's case in the light of the explanation to Rule 9, as interpreted by our High Court in the Shreenivas Cotton Mills case, it becomes clear that the decision of the Gujarat High Court is not inconsistent with the judgment of the Supreme Court in Wallace Flour Mills case. We, therefore, do not accept the contention of Mr. Sethna, for the appellants that the decision of the Gujarat High Court in Aryodaya Spinning Company's case must be deemed to have been overruled by the subsequent judgment of the Supreme court in Wallace Flour Mills case.

16. The explanation to Rule No. 9, as interpreted by the Division Bench of our High Court in Shreenivas Cotton Mills case, makes it clear that the yarn in question shall be deemed to have been removed "immediately before such consumption or utilisation" and the duty payable thereon would be in accordance with the notification which was operative as on such date of removal. In the present case, on the showing of the appellants themselves, as indicated in the show-cause-cum-demand notice dated 19th May, 1979, the yarn in question had been removed from the Department in which it was manufactured and was lying in other Departments. In other words, it was already subject to the process of consumption or utilisation as understood within the meaning of the explanation to Rule 9. Thus, the levy of excise on such yarn would be governed by the notifications which held the field as on the date prior to 15th July, 1977. Since the operative notifications between the period of 18th June, 1977 to the mid-night of 14th/15th July, 1977 exempted the yarn in question from duty, the attempt on the part of the Government to impose duty thereupon by virtue of the Notification No. 226 of 1977 was, therefore, rightly held to be an attempt to levy duty retrospectively on the yarn in question which was wholly exempt from duty when it was manufactured upto and including the time of its removal. Thus, in our view, the judgments of the single Judge under appeal and of Pratap, J. in Miscellaneous Petition No. 215 of 1978, are correct and are quite consistent with the law laid down in the Wallace Flour Mills case, taking into consideration the newly added explanation to Rule 9. We, therefore, have no hesitation in rejecting the second contention of the appellants.

17. Turning to the last contention of Mr. Sethna that the first respondent had not complied with the procedure of removal of the goods, we are of the view that it is unnecessary for us to go into the said question for the disposal of the present appeal. The present appeal arises out of the successful challenge to the show-cause-cum-demand notice issued to the first respondent and if

there is any substance in the grievance made, namely, that the first respondent had not complied with the rules with regard to removal of the goods, the first respondent could have been dealt with according to law. The Department, however, has chosen to issue them a show-cause-cum-demand notice on a particular basis which is really the subject matter of the present appeal. We decline to express any opinion on this grievance of the appellants and leave them to their recourse in law, if any.

18. In the result, the appeal fails and it is hereby dismissed with no order as to costs in the circumstances of the case.

19. Mr. Sethna, the learned counsel for the appellants, orally applies for leave to appeal. Leave refused.

Cases Referred.

11989 (44) E.L.T. 594