

Commissioner of Customs and Vs. Saibaba Ship Breaking

Commissioner of Customs and Vs. Saibaba Ship Breaking

SooperKanoon Citation : sooperkanoon.com/24476

Court : Customs Excise and Service Tax Appellate Tribunal CESTAT Mumbai

Decided On : Jul-13-2001

Reported in : (2003)(90)ECC447

Appellant : Commissioner of Customs and

Respondent : Saibaba Ship Breaking

Advocate for Def. : Mr. A.D. Maru, Mr. M.C. Dhruve

Judgement :

1. The respondents to these applications, except Chaudhry Industries, are represented before us by counsels. After hearing parties on the stay applications filed by the department we have, with their consent, decided to take up the appeals themselves for disposal.

2. Each of the responders was at the relevant time engaged in breaking up of ships. That is to say, it imported a ship, beached it at Port Alang removed from it salvageable materials and parts, and thereafter reduced the ship to scrap, such scrap being cleared on payment of excise duty applicable to the appropriate headings any of the chapters from 72 to 81 of the tariff. Each of these Chapters is for metals and their products and contains a heading for goods and materials obtained by breaking of ships and other floating structure. Almost without exception, the contract entered into between the purchaser and the seller specifies that the ship is to be brought to Alang by the sellers and then delivered to the buyer. The ships that are to be broken almost invariably sail into the port under

their own motive power. The ships therefore contain in addition to fuel and oil required for running the ship's engine and other machinery food, drink and other stores for consumption by the crew.

3. Before the ship is broken up, the fuel and stores are removed on payment of appropriate duty of customs, including additional duty of customs. The question for consideration in these appeals is whether the ship-breaker could take such duty as modvat credit to be used towards payment of duty on goods and materials obtained by breaking up of ship.

4. The matter appears to have its genesis in the circular dated 23.10.1997 of the Ministry of Finance and therefore it is necessary to reproduce it in full: "In the budget of 1995, ship breaking activity was defined as an activity of manufacture by virtue of Note 7 in Section XV of the Schedule to the Central Excise Tariff Act, 1985. Consequent to these two questions arose: (i) Whether the items emerging during the course of ship breaking falling outside the ambit of Section XV of the Schedule to the Central Excise Tariff Act, 1985 would be treated as excisable and are chargeable to Central Excise Duty.

(ii) Whether a ship breaker who has paid CVD would be entitled to modvat credit of the entire CVD paid on the ship or credit will have to be restricted to the extent of inputs contained in goods and materials falling under Section XV of the Schedule.

"2. Director General of Inspection has conducted a study on this issue and a view has been taken that the goods and materials recovered during the course of ship breaking which are outside the ambit of Section XV of the Schedule to the Central Excise Tariff Act, 1985, are non-excisable goods as there is no entry in the Tariff which describes the act of obtaining these items as an activity of manufacture. Moreover, entire ship except ship stores classifiable under 8908 is an input taking part in the activity of ship breaking under Rule 57A of the Central Excise Rules, 1944.

"Hence, the provisions of Rule 57C of the Central Excise Rules regarding the non-admissibility of Modvat credit of duty paid on inputs going into finished excisable

goods which are exempted from payment of duty or chargeable to nil rate of duty will not apply in the case of non-excisable goods.

"3. Accordingly, I am directed to say that the entire credit will be available in this case and no reversal is warranted.

"5. All pending disputes may be resolved in light of aforesaid clarification." 5. The ship-breakers interpreted this circular to mean that the additional duty of customs paid on fuel, oil and other stores contained in the ship, which is generally referred to as bunkering stores, would be available to them as modvat credit for utilisation in payment of duty on goods and materials obtained by breaking up the ship. They therefore took the credit of such duty. The department objected to this by issuing notices. Adjudicating on these notices, the Assistant Commissioner passed orders denying the credit and imposing penalty. On appeals by the ship breakers, the Commissioner (Appeals) set aside the orders of the Assistant Commissioner and held that credit could be taken of the duty paid on such stores. The department has questioned this finding in the appeals before us. We are not concerned with the other issue which arose in the adjudication and appeal proceedings relating to the levy of special additional duty of customs. The department's appeals do not challenge the Commissioner's finding in this regard.

6. The orders of the Assistant Commissioner are similarly worded and contain the same reasoning. The Assistant Commissioner has advanced the following reasons for his conclusion. Note 9 to Section XV provides that the process of breaking of a ship or a floating structure for obtaining materials amounts to manufacture. The value of the ship that is assessed to duty does not include the value of the fuel and oil which are separately cleared on payment of duty. The fuel and oil "is not an input for the purpose of the activity of ship breaking and therefore the CVD paid on such remaining bunkers and oils would not be entitled for modvat credit." He has imposed penalty on his finding that the ship breaker was not entitled to take credit in the light of such a clear position in law. The Commissioner (Appeals)'s common order disposes of appeal against all the 36 orders. The reasoning that the Commissioner (Appeals) advances for setting aside the orders of the Assistant Commissioner is as follows: According to the Board's circular 37/96 dated

3.7.1996 the bunkers, fuel oil and other ship stores are not imported separately and as part of ship stores when imported. He says: "It is a fallacious argument that the appellants had filed a separate Bill of Entry for these items and, therefore, these were imported separately. The only reason for this segregation is over classification and assessment. As the entire ship has been accorded the status of an input and CVD is also paid on the entire ship, credit of CVD so paid will be available to them as it has been well settled proposition of law that entire ship participates in the activity of ship breaking (manufacturing activity)" He also finds that the Board's circular dated 23.10.1997, which we have reproduced above, supports his reasoning. He says: "the Board has by way of this Circular specifically excluded the operation of Rule 57C in respect of this particular activity i.e., ship breaking activity and has gone on to clarify that notwithstanding the status of goods that fall outside the parameters of Section XV including the ones under consideration (non-excisable), the entire quantum of CVD paid on the ship imported for breaking will be available and no reversal is warranted. Once the operation of Rule 57C has been ruled out, I don not find any merit in denying the credit of CVD paid by the appellants on the entire ship, imported them for breaking." 7. His attention was drawn to the circular 37/96 dated 3.7.1996 of the Ministry of Finance, Department of Revenue. This circular an opinion of the World Customs Organisation, Brussels on the question referred to it by the Government of India, of classification of movable gears such as lifting and handling machinery, bunkers such as fuel oil and engine oil and ships stores such as spare parts, food stuffs and other beverages, etc., imported on board a ship for breaking up. The reference to the World Customs Organisation was made following an objection by audit that these goods would not be classifiable under heading 89.08 of the Customs Tariff as ships and floating structures for breaking up, but on merits. The circular communicates the acceptance by the government of the view of the World Customs Organisation that fuel and oil contained in the vessel's machinery and engines would be regarded as forming an integral part of the vessel and classifiable under heading 89.08 but other remaining fuel, oil and ship stores were classifiable in their own appropriate heading. The Commissioner (Appeals) finds that, on the principle that a later judgment of a court is to be applied in preference to an earlier judgment of the same court on the same issue, the latter circular of

23.10.1997 takes precedence over this circular of 1996.

8. The department's appeal first urges that the circular dated 28.3.1997 provides that the bunker stores and foodstuffs are not inputs and therefore duty paid on them is not available as credit. It relies heavily upon the circular 37/96 dated 3.7.1996 indicating the opinion of the World Customs Organisation as to the classification of the fuel oil and other stores. It contends that the unvarying practice, formalised in the memorandum of undertaking between the Gujarat Maritime Board (which has leased the yards where the ships are broken up by the ship breakers) and the Ship Breaker's Association also provides that the ship's tanks containing oil and fuel tank, etc., should be emptied and evacuated before breaking up of the vessel commences. Therefore, it is only the ship without the fuel, oil and such goods on it which is broken into and is therefore the starting point of the manufacture.

9. Mr. A.D. Maru, counsel for respondents in 11 appeals, says that he does not wish to challenge the claim in the department's appeal that credit cannot be taken of the duty paid on foodstuff and other such stores. His claim is limited to duty paid on bunker in stores such as fuel and lubricating oil. He contends that these are necessarily part of a ship. The ship cannot sail and reach the ship-breaking yard unless these are present on board. What was imported therefore is a ship complete with these stores which are a part of it. The Board's circular of 1997 makes it clear that the duty paid on these stores would be available as credit. He also relies upon the observation of the Supreme Court in paragraph 5 of its decision in *Tata Engineering & Locomotive Company Ltd. v. State of Bihar* 10. Mr. M.C. Dhruve, counsel for respondents in 24 appeals out of the remaining 25, contends as follows in his own words: The entire ship including the fuel oil and the other consumable stores such as food stuff, is one entity and takes part in manufacturing activities.

Therefore, the entire ship has to be considered an input under Rule 57A. The circular of the Board of 1997 provides that these stores are non-excisable although the reason for this is that they are emerged as a result of manufacturing activity.

11. The contentions in the written submission filed by Chaudhry Industries are these: When the ship is imported for breaking up, these goods as defined in Sub-section (2) of Section 22 of the Act form part of the ship and are therefore part of the inputs. The agreement between the buyer and seller of the ship stipulated that the ship is to be delivered as-is-where-is condition i.e., floating on the sea. The Board's circular of 23.10.1997 has been misinterpreted by the appellant, the tanks of the vessel form an integral part of the ship and therefore the fuel contained in the ship is classifiable in heading 89.08. Quasi-judicial authorities are not bound by the administrative instructions or clarifications as held the Supreme Court and therefore the Commissioner's arguments are not maintainable. It is also contended that the latter circular of the Board has to be applied in preference to the other.

12. We will now consider the two circulars of the Board. They essentially seek to answer the same question - whether the goods which are imported as a result of ship breaking which do not fall for classification under Section XV of the Tariff would be treated as excisable goods and are liable to excise duty and whether the additional duty of customs paid on them would be available as modvat credit or the credit will have to be restricted to the extent of inputs contained in goods and materials falling under Section XV of the tariff. We will first consider the latter circular. The circular says that the goods and materials recovered from the ship breaking which are not classified under Section XV "are non-excisable goods and there is no entry in the tariff which describe the ambit of obtaining these items as an activity of manufacturing". The entire ship, including the goods ship's stores and consumables, would be therefore classifiable under heading 89.08. Hence the provisions of Rule 57C will not apply in the case of non-excisable goods.

13. We must confess that the terminology employed in the circular is confusing and unclear. It appears to us that the second question that it seeks to answer is whether the ship breaker would be entitled to utilise the entire additional duty of customs paid on the ship or only that portion of the additional duty representing the ship, breaking of which results in goods classifiable under Section XV of the Act.

Section XV covers Chapter 72 to 81. In each of these there is goods, materials obtained by breaking up of ship. The Directorate General of Inspection has apparently concluded that the goods obtained as a result of ship breaking which are outside the ambit of Section XV are non-excisable goods. These other goods would be parts of the ship such as chain, capstan, etc., which are removed and sold as such before the remainder of the ship is broken as scrap. His conclusion that these goods are non-excisable goods, because there is no entry in the tariff which described ambit of obtaining these items as manufacture is again confusing. The term "excisable goods" is defined in the Central Excise Act as meaning goods specified in the First schedule and second Schedule to the Central Excise Tariff Act, 1985 as being subjected to a duty of excise. It would therefore not correct to say that such parts are not excisable goods. To say that would mean that they are not liable to duty of excise after their manufacture. They are clearly excisable goods. What the Director General of Inspection no doubt, meant to say is that these goods are not the result of the manufacture and therefore not liable to duty. Removal of a part from the ship is not the result of the manufacture. There had been doubts expressed whether reducing the ship to scrap would amounts to manufacture. This doubt now settled with the insertion of note 7 to Section XV. It would be not correct to say that this conclusion would apply with equal force to bunker, oil, stores, etc. Their removal is not an act of manufacture and no excise duty is liable to be paid on them. This was in fact the basis of the Tribunal's decision in Priya Blue Industries Ltd and Ors.

v. CCE (appeals E/1194/2000 and Others). The question there was the eligibility to the ship breakers to reverse the modvat credit which they on their own debited by applying the provisions of Rule 57CC, which requires the manufacturer to make deposit of 8% of the value of the non-excisable goods in case he utilises common inputs for manufacture of such goods and excisable goods.

14. It is therefore not possible to see how the contents of the circular provided any support for the proposition that modvat credit can be taken of the duty paid on the stores. The circular itself says that the entire ship except ship stores are classifiable under heading 89.08 clearly indicating that such stores are not classifiable under heading 89.08.

15. The earlier circular No. 37/96 which reproduces the opinion of the World Customs Organisation, had dealt with the classification of the ship stores such as spare parts, food stuff, alcohol and other beverages and bunkers, fuel oil, engine oil. The circular dated 27.10.1997 is with reference to Central Excise duty. For the true meaning of the term "ship stores" we have to consider the provisions of Customs Act, 1962. Sub-section (38) of Section 2 of the Act defines "stores" to mean "goods for use in a vessel or aircraft and includes fuel and spare parts and other articles of equipment, whether or not for immediate fitting". 'Stores' therefore includes the goods that we are concerned with - fuel oil, and other foodstuffs, etc. Therefore the words "ship's stores" in the Board's circular of 1997 must be given the meaning as contained in the provisions of law that deals with such goods in the Customs Act. It would then follow that these goods are not classifiable under heading 89.08 as ships for breaking up.

16. There is, in any case, no dispute on this latter ground. The departmental representative's contention that the statement that the fuel oil and other such stores were assessed on their merit under heading 89.08 for payment of custom duty including additional duty is supported by bill of entry that is produced and is not challenged seriously by the counsel for the respondent. Therefore these goods have paid duty including additional duty not as a ship entered for breaking up but on their own merit as ship stores.

17. The Commissioner (Appeals) has completely overlooked these facts.

Nor is it possible to accept his view that because the ship carried on it the fuel and other stores must be considered to be part of that ship. It is an extreme proposition to say that anything on board a ship, even if required for the operation, thereby becomes part of it.

By this criteria, petrol and oil in a car become part of a car. Fodder kept in a bullock car to feed the bullocks that draw it becomes part of the cart. This is an obvious an untenable proposition.

18. There is also no question of preferring a latter circular to an earlier circular. The two circulars were issues for two different issues. One on the classification for

customs purpose of fuel oil, etc., and the other availability of credit. They may impeach upon each other but very independent and separate.

19. Nor are we able to accept the contention that the fuel oil and other such items arose during the course of manufacturing activity i.e., breaking up of ship. We have clearly found that removal of stores from ship is not a manufacturing activity. Considering that fuel and other stores necessarily required to be removed for the purpose of safety and efficient operation apart from the legal requirement of the Gujarat Maritime Board, how it could be said these are the result of breaking up is beyond our capacity to understand. It would not be correct to say that the activity of breaking up of ship commences as soon as it enters the port. It is only when the workmen concerned commence breaking it using the machinery required for the process that the manufacture has begun.

20. The paragraph 5 of the Supreme Court judgment referred to by Mr.

A.D. Maru were concerned with interpretation of the word 'raw material' occurring in Bihar Finance Act, 1981. In paragraph 4 of the judgment the Court relied upon its own judgment in Collector v. Jay Engineering Works Ltd. 1989 (39) ELT 169 whether nameplates used by the manufacturer of fans would be inputs of fan for the purpose of notification 201/79. The Court said that the use of the word indicated that the benefit of the notification 201/79 was intended for every item which is raw material in the widest sense made wider by using the expression "input". The decision therefore is not really relevant to the facts before us.

21. Apart from that it obviously cannot be said that fuel oil and foodstuffs are input required for manufacture of scrap. They are not used directly or indirectly in or in relation to the emergence of scrap. Scrap can emerge without these being present. On the other hand their presence may immune emergence of scrap.

22. Accordingly we hold that respondents were not entitled to take credit of the duty paid on the fuel, oil and other oil, food stuffs (other than the fuel, oil contained in the ship's engine and machinery). The departmental representative says it is not the intention of the department to deny credit to such fuel and oil.

23. We however, do not find that there was a case for imposition of penalty. As we have noted the circular of the Board is ambiguously worded and could have given rise to the views that the respondents held. Further there is no finding or allegation that the respondents knowingly set out to take credit in defiance of law. We therefore set aside the Commissioner (Appeals)'s order except that part of the order setting aside the penalties imposed on the respondents and restore the orders of the Assistant Commissioner to the extent that they deny the credit on the goods under consideration.

SooperKanoon - India's Premier Online Legal Search - sooperkanoon.com