

Diamond Clock Manufacturing Co. Vs. C.C.E.

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Court : Customs Excise and Service Tax Appellate Tribunal CESTAT Delhi

Decided On : Dec-30-1987

Reported in : (1988)(15)LC57Tri(Delhi)

Appellant : Diamond Clock Manufacturing Co.

Respondent : C.C.E.

Judgement :

1. These two appeals, involving common question of facts and law were heard together and are being decided together. The appellants, stated to be a limited company, manufacture, inter alia, rickshaw and taxi meters. They appointed M/s. Anand Traders, a partnership concern as their distributors throughout India. The appellants also directly sell their meters to Industrial consumers like Bajaj Auto Limited. Shri U.V.Vaidya, Managing Director of Diamond Clock Manufacturing Co. Pvt. Ltd. thereafter referred to as Diamond) holds about 12% of shares in Diamond and 75% interest in Anand Traders. Shri Vaidya's mother holds nearly 25% of interest in Anand Traders and about 48% shares of Diamond. The sale pattern of Diamond is that 70% of their production is sold to Anand Traders and 30% to others. The prices charged by Diamond to Anand Traders are, on an average, about 9.17% less than the prices to others.

2. The Collector of Central Excise issued a show cause notice to the appellants threatening to cancel the concession of assessment on invoice price under Notification 120/75-CE, which was granted to them and proposing assessment of the goods under S. 4 of the CES Act. This value was to be worked out on the

basis of the sale price of Anand Traders to their customers. He alleged that both Diamond and Anand Traders were one and the same unit and that the two units colluded with each other, manufactured and cleared excisable goods without paying duty on the prices charged by Anand Traders to their customers. It was alleged that these deeds were done knowingly and that the appellants suppressed facts deliberately without disclosing them to Central Excise Department.

The Collector besides asking them to show cause why the concession granted under Notification No. 120/75-CE should not be withdrawn, also asked them to show cause why differential Central Excise Duty for the period 1.10.1980 to 30.9.1985 should not be recovered from them and why they should not be penalised.

3. After due process the Collector passed orders confirming the demand for differential duty of Rs. 8,55,457 raised in the show cause notice and imposing penalty of Rs. 1,45,000/- on the appellants. Hence this appeal. In another proceedings in Appeal No. 660/86-A before us the Collector ordered recovery of Rs. 2,04,292/- on certain amounts not included in the value of the goods and also imposed a penalty of one lakh of rupees.

4. We heard Shri N.D. Khosala, learned Consultant for the appellants.

Shri. Khosala, after explaining the constitution of the two units submitted that in terms of Section 4(4)(c) of the Central Excises & Salt Act these two were not related persons. He submitted that it is entirely wrong to say that the two units are one and the same. He emphasised that three out of the four Directors of Diamond had nothing to do with Anand Traders. They are not related to Shri Vaidya, the Managing Director. He argued that the use of common facilities by two units does not render them related persons and relied on the judgment of Cegat in *Hagjivandas & Co. Thane v. Collector of Central Excise, Bombay-II* reported in 1985 (19) ELT 441 (Tribunal) and pleaded that the facts of the present matter are on all fours with that case.

5. Referring to the lower prices at which the meters were sold by Diamond to Anand Traders, Shri Khosala argued that the difference was only 9.17% and was

not unduly high. Explaining the difference in prices, he submitted that the meters sold to M/s. Bajaj Auto are used by them directly and they were not incurring selling expenses. In this context, he relied on the judgment of the Government of India in Delton Cables Industries (P) Ltd. reported in 1978 (2) ELT (3 661).

6. Shri Khosala went on to argue that the crucial test to decide whether or not the two units were related persons was that of mutuality of interest. He submitted that there is neither any allegation nor any proof of such mutuality of interest between the two units. In support of his arguments, he relied on the judgment in the Facit Asia Ltd., Madras v. Collector of Central Excise, Madras reported in 1985 (21) ELT 711 = 1985 (5) ETR E12. He submitted that the Collector did not consider all the points made by the appellants before him especially the one which related to mutuality of interest.

7. The learned Consultant argued that the two units in question were separate legal entities and not one and the same. He cited Madras High Court judgment in Bapalal and Co. (Manufacturing) v. 1. The Secretary to the Government of India, Ministry of Finance Department of Revenue, New Delhi. 2. The Appellate Collector of Customs, and Central Excise, Madras-1. 3. The Assistant Collector of Central Excise, Madras-1, reported in 1981 ECR 279D (Madras) and the judgment in Aroma Apparels, Bombay v. Collector of Central Excise, Bombay reported in 1986 (25) ELT 90 (Tribunal).

8. Shri Khosala submitted that the Collector wrongly held that Anand Traders was created for the purposes of evading Central Excise duty.

This firm was founded in 1963 whereas the Central Excise duty under Tariff Item 68 was introduced in 1975. Citing a decision of the Supreme Court in MacDowell and Co. Ltd. v. Commercial Tax Officer (1985 I.T.R. page 148 (referred to by the Collector in his orders), the learned Consultant argued that tax avoidance within law is not evasion.

9. Advancing alternative arguments Shri Khosala submitted that the cost of bought-out items purchased by Anand and supplied to their dealers was not includible. These items were cable, bracket and adaptors. These are not

manufactured by the appellants and incomplete machines are cleared from the factory without these items. He also submitted that the duty was demanded under Rule 9(2) read with Section 11A by show cause notice dated 3.12.1985. He submitted that there was no clandestine removal in this case and therefore invoking Rule 9(2) was totally wrong. There was no allegation of clandestine removal in the show cause notice according to him. He also denied suppression of facts and submitted that no requirement of law was violated by the appellants.

10. Shri Khosala further pleaded that the price at which Anand Traders sold the goods included excise duty and sales tax and these two elements were not excluded when calculating the duty as demanded by the Central Excise department. This aspect, according to the learned Consultant, was not at all discussed by the Collector. Finally, Shri Khosala submitted that there was no intent to evade duty and there was no Mens Rea. Therefore there was no justification for imposition of penalty.

11. Shri S. Krishnamurthy, the learned SDR, submitted that as the appellants removed the goods without payment of correct duty, there was clandestine removal warranting the invoking of Rule 9(2) Central Excise Rules and imposition of penalty. He submitted that the appellants paid duty on the invoice value instead of on the value under Section 4, Central Excises and Salt Act. He further argued that the two units are related persons as between the mother and son they owned Anand Traders, held 60% shares of Diamond and Shri Vaidya was the Managing Director of Diamond. In support of his arguments he cited the judgment of the Supreme Court in Union of India v. Bombay Tyre International [1983 (14) ELT 1896 (S.C.) (paragraphs 46 to 48] as also Moped India Ltd. v. Assistant Collector of Central Excise, Nellore reported in 1986 (23) ELT 8. Further he cited Joint Secretary to Government of India v. Food Specialities Ltd. reported in 1985 (22) ELT 324 (SC) and a decision of the Supreme Court reported in 1985 (22) ELT 236 (Tribunal) - Bengal Paper Mills, Calcutta v. Collector of Central Excise, Calcutta. He, however, agreed that while computing value under Section 4 of Central Excises and Salt Act, Excise duty and Sales Tax were to be conducted.

12. In his brief rejoinder, the learned Consultant submitted that the case law cited by the learned SDR was not applicable to the facts of the present matter. He argued that the two units cannot be relatives as only individuals can be so. He pleaded that clandestine removal is a physical activity and filing a wrong price list does not amount to clandestine removal. He also pleaded bona fides on the part of the appellants.

13. We have considered the arguments of both sides. Before proceeding further we would like to discuss, in passing, the appellant's argument that there is no question of related person in this case as both the units involved are not individuals but consist of a limited company and a partnership. We do not consider that the word "related person" occurring in Section 4(4)(c) should be given such a narrow restricted and unrealistic interpretation. It is clear from the very wording of the sub-section that a related person would consist of a company also.

"Related person" means a person who is so associated with the assessee that they have interest, directly or indirectly, in the business of each other and includes a holding company, a subsidiary company a relative and a distributor of the assessee, and any sub-distributor of such distributor." The relevant thing to be examined here is whether or not the appellants and Anand Traders are covered by the first part of the definition. In other words the question is whether Anand Traders are so associated with the appellants that they are interested, directly or indirectly, in the business of each other. It was repeatedly argued before us that the two companies are separate in the eyes of law. It was emphasised that they are separately registered and are treated as separate units for the purpose of various Acts. We do not consider that it is necessary to go into this assertion. However, the question before us is not whether they are one and the same but whether they have mutual interests, and more particularly, whether the appellants can be permitted to avail of Notification No. 120/75-C.E. This notification contemplates the non-existence of any commercial, financial or other relationship except that created by the sale of the goods. Therefore, it is in the light of this notification that we have to examine the relationship between the two parties.

15. Admittedly, Shri U.V. Vaidya, Managing Director of Diamond Clock Manufacturing Co. Pvt. Ltd.; holds 12% of shares in the company and has 75% interest in Anand Traders. His mother has another 48% interest in the same company and 25% interest in Anand Traders. In other words between Shri Vaidya and his mother they fully owned the firm Anand Traders and the two together held the controlling interest of 60% in Diamond. This two-way financial interest alone renders the two units related persons under Section 4(4) and establishes identity of interests between the two. However, a perusal of the impugned order shows that the Collector has taken into consideration various other factors also. We observe that the two units have common staff and common office and have common records room. Further, both units used a common telephone and there is a common electric meter for each office.

The appellants cited case law to show that these circumstances should not lead to a conclusion that the two units in question were one and the same. We note their arguments but observe that the appellants also sell 70% of their production to Anand Traders and the price to them is over 9% less as compared to their price to others, especially Bajaj.

16. We have considered the case law cited by the appellants where such case law appeared to be relevant. In Bapalal and Co. case (supra) the Madras High Court held that the two registered companies are separate legal entities even if all the partners in one are also partners in the other. Similarly, in Delton Cable Industries Ltd. the Government of India held that though the Directors in the two companies were common, the two units in question were separate firms. In Industrial Engineering v. Collector of Central Excise, Chandigarh cited by the appellants the CEGAT ruled that where all the partners are common in different firms, each such partnership is a separate legal entity for the benefit of the Notification 89/79-C.E.17. We refer to these judgments, as reference was made to them by the appellants. As mentioned earlier the question before us is not whether the two units are different legal entities or not. The question is whether in terms of Notification 120/75-C.E. there is any relationship between them that disentitles them to the concession. We have referred above to the various other circumstances that came to our notice and to the notice of the Collector. Each of

them separately may not lead one to a conclusion that the two units in question are related persons. But taken together cumulatively they lead us to the conclusion that there was mutual interest between them. We have already noticed the financial set up of the two units detailing the share holding and interest of Shri U.V. Vaidya and his mother in the two units. The additional facts of sharing of common accommodation, telephone, a lower price and financial interest in the shape of holding the majority shares in Diamond by Shri Vaidya and his mother while fully sharing Anand Traders and the other enumerated circumstances cannot be wished away with such close financial and other involvement, the price charged by Diamond from Anand could not be considered at arm's length. The Ld. SDR cited some case law in support of his argument that the two units are related persons. However, no judgment cited by him was found to be directly applicable to the facts of the present case.

18. The appellants advanced an argument that a difference in sale price upto 10% in the sale by the manufacturer to a dealer should be ignored and cited the Delton Cable Industries case in support of their argument [1978 (2) ELT (3 661)]. We have perused this judgment, an order in Revision by the Government of India. This observation by the two Joint Secretaries is confined to the facts of that case which are different from the present ones. There is no general proposition and this finding is not backed by any judgment of the High Courts or the Supreme Court; besides, the order pertained to the admissibility of a discount. This judgment is, therefore, not applicable.

19. It is the totality of the circumstances that must be examined in a situation like the present one. True, Anand Traders was already in existence as distributor for Diamond long before the Central Excise duty became leviable on their product. All the same when we take all the facts together, facts as enumerated in the earlier paragraphs, which were not disclosed to the Central excise authorities, the conclusion that the close mutuality of interest between the two units was suppressed from the authorities is obvious. We therefore uphold the conclusion of the Collector in this regard.

20. Notification No. 120/75-C.E. contemplates, inter alia, that the exemption shall be available only if the invoice price is not influenced by any commercial, financial or other relationship whether by contract or otherwise than the relationship created by sale of the goods. Our earlier discussion shows that the relationship between the appellants and the Anand Traders cannot be described as an independent one. If there is any doubt left about the relationship between the two firms and the mutuality of interest between them, it would be dispelled by a perusal of three undated letters from appellants to Anand Traders whereby in the name of "Rate difference on sales made" (to Anand Traders) the appellants simply charged them Rs. 2 lakhs, 4 lakhs and Rs. 3.09 lakhs. Copies of these undated letters were filed by the appellants and seem to pertain to the years 1982, 1981 and 1980; except for the figures and items the letters are similar. We reproduce below one letter to illustrate the relationship between the two parties and the nature of transaction referred to.

We have charged you rate difference on sales made to you during the calendar year 1981 on fare-meters, because it is not possible for us to afford the prices charged earlier.

Item Nos.

per meter (Rs.)	Amount (Rs.)	Rickshaw Meters	4737	72	3,41,064.00	Taxi Meters
395	145	57,275.00	UT/TP Meters	25	66	1,650.00

_____ We confirm the above entry in our books of accounts.

Thanking you, 21. There can be no better comment on the financial interest of the appellants in Anand Traders, viewed in the background of the investment made by Shri Vaidya and his mother to which we had referred earlier in this order. In this context we have respectfully referred to the judgment of the Supreme Court in Mohan Lai Madan Lai Bhavasar and Ors.

v. Union of India and Ors. reported in 1986 (23) ELT 3 (S.C.) wherein the Supreme Court had the occasion to examine a similar question concerning two firms one of which was the Chief Distributor of the products manufactured by the other. The Supreme Court held that the firm of M/s. Mohanlal Madan Lal Bhavasar & Sons,

though a separate partnership firm was in fact a firm in which not only the original first appellant and Ors. were partners but a son of which was also a partner. The Hon'ble Supreme Court held that there was thus an identity of interest between the firm of M/s. M.B. Bhavasar & Sons and M/s.

Bhavasar Chemical Works. The circumstances in that case are to a large extent similar to those of the two present matters before us. Keeping all these facts in mind we hold that the appellants were correctly held not to be eligible to the concession of Notification No. 120/75-C.E.22. The next question that arises is the value for assessment.

Obviously the price at which Anand Traders sell the goods should be the price from which the assessable value should be calculated. As argued by the learned Consultant for the appellants some deductions have to be allowed from the sale price of M/s. Anand Traders before the assessable value can be arrived at. We discuss the various items and giving our orders on each of the items.

The appellants submitted that more than 50% of their sales are in initial packing only and not in wooden crates. The question of secondary packing is a well settled matter now and the Tribunal has passed a number of orders following the Supreme Court decision in Union of India v. Bombay Tyre International and Ors. [1983 (14) ELT 1896]. We also followed the judgment of the Supreme Court in Union of India and Ors. v. Godfrey Philips India Ltd. and Ors. reported in 1985 (22) ELT 306 (S.C.). The matter may be decided in the light of these judgments.

If by arrangement and according to the condition of sale interest has to be paid on delayed payment, such interest should not be included in the assessable value. The Supreme Court orders in ACCE v. MRF, reported in 1987 (27) ELT 553 should be followed in this regard after verifying the facts.

The Supreme Court has held, quite clearly [1987 (27) ELT 553 (S.C.)] - Assistant Collector of Central Excise and Ors. v. Madras Rubber Factory Ltd. and Ors. that it is only those expenses incurred on account of factors which contributed to its value upto the date of sale or the date of delivery which are liable to be included in the assessable value. Therefore, if the expenses are incurred, only after sale or

delivery, these need not be included. The appellants' claims will have to be examined in the light of the judgment of the Supreme Court.

The appellants pleaded for deduction of testing charges in respect of meters sold by them. Testing of meters before delivery is a basic and normal duty of the manufacturer. The shifting of the charges to Anand Traders is clearly only a colourable device to evade payment of duty on such charges. We, therefore, reject this request.

Similarly, passing on the warranty charges is also not legal. The manufacturer is responsible for the warranty and the expenses incurred for the same should be included.

23. The appellants claim that Anand Traders have supplied bought-out items to their customers. These consisted of cable, bracket and adopter. It appears that these three are essential for the operation of the meter but they are not manufactured by the appellants nor are they fitted into the machines before clearance. If this is the factual position and only incomplete machines are cleared from Diamond's factory, the value of such parts supplied to customers by Anand Traders later should not be included.

24. The request for deduction of Excise duty and Sales Tax from Gross price is reasonable and has the sanction of law.

25. To clear any possible doubts, we observe that in respect of sales made to Bajaj and other industrial consumers as a separate class of buyers, the assessable value will have to be calculated with reference to proviso (i) to Section 4(l)(a). It is only the sales to Anand Traders that will come into the purview of proviso (iii) to Section 4(l)(a).

26. It has been extensively argued by the learned Consultant for the appellants that the extended period of limitation should not be applied to the appellants. We have considered this plea. We have also examined the provisions of Notification No. 120/75-C.E. The appellants availed of the concession without disclosing the facts and details of the cross share holding by, Shri Vaidya and his mother in

Anand and Diamond.

Keeping in mind the provisions of Notification No. 120/75-C.E. we hold that this is a clear case of suppressing information with a view to evade payment of full excise duty. We had earlier referred to three debit notes each for lakhs of rupees. The appellants passed on the legitimate duty of manufacturer (testing for quality and grant of warranty) to Anand. Viewing all these facts together we hold that there was Mens Rea and there was deliberate suppression of facts, we, therefore, uphold the extended period of limitation for this demand.

27. In this view we order that (i) the differential duty payable by the appellants should be re-calculated on the basis of our observations made above. Where we have not indicated anything, the claim for deductions will be decided on the basis of the judgments of Supreme Court and High Courts, (ii) The assessable value in respect of clearances to Anand should be revised in the light of our orders, (iii) Before revising the demand for differential duty the appellant should be given an opportunity to represent so that their claims are taken note of, examined, and disposed of according to law.

28. There are two penalties on the appellants amounting to Rs. 2,45,000.00. We note that some of the demands overlap and some legitimate deductions have not been granted. Taking all circumstances in consideration we reduce the penalties of Rs. 1,45,000/- and Rs. 1,00,000/- imposed in the two cases to Rs. 100,000/- and Rs. 50,000/- only, in the two appeals respectively.

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