

Collector of Central Excise Vs. Paper Packing Industries

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Court : Customs Excise and Service Tax Appellate Tribunal CESTAT Delhi

Decided On : Apr-21-1988

Reported in : (1988)(17)ECC137

Appellant : Collector of Central Excise

Respondent : Paper Packing Industries

Judgement :

1. The question for decision in these appeals by the Revenue is whether for judging the respondents eligibility to benefit of exemption under Notification 105/80, dated 19.6.1980, the value of clearances of the two respondents should be clubbed.

2. After following the usual procedure the Assistant Collector of Central Excise Division Srinagar by order dated 7.10.1983 held that the clearances of the two respondents should be clubbed and that they are not eligible to separate exemption. He confirmed the demand of duty Rs. 73719.75 raised in the show cause notice. In appeal, however, by the respondents (appellants before him) the Collector of Central Excise (Appeals) New Delhi by order dated 8.3.1984 following the decision of this Tribunal in G.D. Industrial Engineers Faridabad v. Collector of Custom & Central Excise. Chandigarh 1983 ELT 1994 (CEGAT) held that even though the two partners of the two respondent firms were common the units were separate and their clearances could not be clubbed. He held them separately eligible to benefit of exemption under Notification 105/80, dated 19.6.1980 to the extent of clearances of Rs. 30 lakhs. He thus set aside the demand and allowed

the appeals.

Aggrieved with this decision the Revenue has filed these appeals to the Tribunal.

3. At the hearing of the appeals Smt. J.K. Chander, JDR for the appellant and Shri Y.N. Chopra, Consultant for the respondents were heard and papers perused.

4. Smt. Chander submitted that the decision of the Tribunal in G.D.Industrial Engineers, Faridabad had been challenged before the Supreme Court and till the matter was decided the Collector (Appeals) should not have hastened into a decision. Shri Chopra relying on the same decision submitted that the Collector (Appeals) was right in holding that the clearances of the two respondents could not be clubbed. The Bench put it to both the parties as to what they had to submit in view of the very recent decision of the Supreme Court in Deputy Commissioner of Sales Tax (Law) Board of Revenue (Taxes) Ernakulam v. K. Kelukutty 1986 (24) ELT 186 (SC). Smt. Chander after going through the decision submitted that the decision of the Tribunal in G.D. Industrial Engineers, Faridabad could not, in view of this decision of the Supreme Court, be said to be sound law and should be taken to have been overruled. Shri Chopra had no particular comments to make though he maintained that the Tribunal decision in G.D. Industrial Engineers, Faridabad was in no way affected by this Decision of the Supreme Court.

5. Before dealing with the merits of the appeal it would be useful at this stage to refer to the notification in respect of which the clearances are sought to be clubbed and the history of the two respondents. Each of the two respondents are engaged in the manufacture of paper packing materials. These materials at the relevant time were falling under Tariff Item 68 though later till 1986 Tariff came into force fell under Item 17(4) during which period each of the two respondents held central excise licence in respect of the products under Item 17(4). The present dispute relates to period when the products fell under Item 68. That earlier on 25.9.1974 a partnership came into existence between Shri Gopal Magotra and Shri Gouri Shankar as partners. After death of Gouri Shankar on 20.12.1976 his son Shri Shrikumar Sharma became partner with Shri Gopal Magotra. The two were to share the profit and loss of the firm in proportion 50: 50. The business of the firm was to continue manufacturing and selling of paper packing materials. The

business of the partnership firm was to be carried at Jammu or at such place or places as may be decided from time to time. On 16.2.1979 another partnership deed between the two above named persons Shri Gopal Magotra and Shri Shrikumar and their wives Smt. Kamal Magotra and Smt. Sudesh Sharma was executed. According to this deed the business of the firm was to be run under the name and style of M/s. Packart. The business of the partnership firm was to be carried at Jammu or at such place or places as may be agreed upon. The profit and loss of the firm amongst the four partners was to be shared 25% each. This firm M/s. Packart between the period 1.4.1981 to 28.2.1982 without payment of duty cleared corrugated board, boxes containers and cartons and the like goods worth Rs. 9,21,496.89. Value of clearances of the other firm M/s. Paper Packing Industries, Gangyal, Jammu during the same period exceeded Rs. 60 lakhs. This firm had availed of exemption to the extent of Rs. 30 lakhs in terms of Notification 105/80, dated 19.6.1980. Show cause notice raising demand Rs. 73,719.75 and alleging that M/s. Packart was not eligible to separate exemption under the notification was issued against the respondents. The two respondents took up pleas like being separately registered industrial units for income-tax and sales tax purposes and therefore their clearances not being clubbable. The result of adjudication and appeal has already been set out above.

6. At this stage it is necessary to briefly refer to the relevant notification. Notification 105/80, dated 19.6.1980 superseding Notification 89/79 dated 1.3.1979 exempted goods falling under Item 68 in respect of the first clearances of the said goods for home consumption by or on behalf of a manufacturer from one or more factories upto a value not exceeding rupees thirty lakhs, cleared on or after the first day of April in any financial year, from the whole of the duty of excise leviable thereon subject to conditions set out therein. The conditions are not material for decision of the present appeals. Notification 89/79, dated 1.3.1979 gave full exemption of similar first clearances upto an aggregate value not exceeding rupees fifteen lakhs and partial exemption on the next clearances of aggregate value of rupees fifteen lakhs subject to certain conditions set out therein which again are not material for the decision of the present appeals. The exemption was to goods cleared for home consumption on or after the first day of April in any financial year by or on behalf of a manufacturer from one or more

factories. This Notification 89/79 superseded an earlier similar Notification 176/77, dated 18.6.1977.

Notification 176/77, dated 18.6.1977, later superseded by Notification 89/79, dated 1.3.1979, exempted goods falling under Item 68 of the CET cleared for home consumption on or after the first day of April in any financial year by or on behalf of a manufacturer from one or more factories from the whole of the duty of excise leviable thereon subject to certain conditions like capital investment on plant and machinery therein. It may be stated that this condition as to investment on plant and machinery is found in all the three notifications and there is no dispute that the respondents in each of the units fulfilled this condition. Under second proviso to this notification the exemption under the notification was to apply to the first clearance of home consumption by or on behalf of the manufacturer from one or more factories upto a value not exceeding rupees thirty lakhs during a financial year subsequent to 1977-78, which period alone is material for decision of the present appeals.

7. The above history of the notifications is set out only to indicate that partnership deed dated 16.2.79 between the four partners (two husbands and their wives) came into existence while exemptions to small scale industries based on value of clearances and investment on plant and machinery were operative. In *Deputy Commissioner of Sales Tax v. K.Kelukutty* 1986 (24) ELT 186 (SC) there are certain observations of the Supreme Court which would have relevance with decision in the present appeals. The Hon'ble Supreme Court after referring to a number of decisions in paras 8,9,10 and 11 of the decision observed as under: "8. As long ago as *Watson and Everitt v. Blunden* 18 Tax Cases 402, *Romer L. J.* said that for taxing purposes "a partnership firm" is treated as an entity distinct from the persons who constituted the firm". This dictum was approved by the House of Lords in *Income Tax Commissioner for City of London v. Gibbs* 10 ITR Supp. 121, and was accepted as good law in India in respect of a partnership firm under the Indian Income Tax Act, 1922 in *A. W. Piggies & Company* (supra).

What that implies is that for the purposes of assessment to tax the income of the partnership firm has to be assessed in the hands of the firm as a single unit, the

first itself being treated as an assessable entity separate and distinct from the partners constituting it. The firm is an assessable unit separate and distinct from the individual partners, who as individuals constitute assessable units separate and distinct from the firm. It is on that basis that the provisions of the tax law are structured into a scheme providing for the assessment of partnership income. We do not think the principle goes beyond the purposes of that scheme. It does not confer a corporate personality on the firm. Beyond the area within which that principle operates, the general law, that is to say, the partnership law holds undisputed domain.

9. Now in every case when the assessee professes that it is a partnership firm and claims to be taxed in that status, the first duty of the assessing officer is to determine whether it is, in law and in fact, a partnership firm. The definition in the tax law defines an "assessee" or a "dealer" as including a firm. But for determining whether there is a firm, the assessing officer will apply the partnership law, subject of course, to any specific provision in that regard in the tax law modifying the partnership law. If the tax law is silent, it is the partnership law only to which he will refer. Having decided the legal identity of the assessee, that it is a partnership firm, he will then turn to the tax law and apply its relevant provisions for assessing the partnership income.

10. The Kerala General Sales Tax Act contains no provision which bears on the identity of a partnership firm. Therefore, recourse must be had for that purpose to the partnership law alone. Where it is claimed that they are not one but two partnership firms constituted by the same persons and carrying on different businesses, the assessing authority must test the claim in the light of the partnership law. It is only after that question has been first determined namely, whether in law there is only one partnership firm or two partnership firms, that the next question arises: whether the turnover is assessable in hands of the partnership firm as a taxable entity separate and distinct from the partners? There is first a decision under the law of partnership; thereafter, the second question arises, the question as to assessment under the tax law. It is clear, therefore, that reference must be made first to the partnership law.

11. The Indian Partnership Act, 1932 has, by s.4, defined a "partnership" as 'the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all'. The section declares further that the persons who have entered into partnership with one another are called individually "partners" and collectively "a firm". The components of the definition of "partnership", and therefore of "a firm" consist of (a) persons, (b) a business carried on by all of them or any of them acting for all, and (c) an agreement between those persons to carry on such business and to share its profits. It is the relationship between those persons which constitutes the partnership. The relation is founded in the agreement between them.

The foundation of a partnership and, therefore, of a firm is a partnership agreement. A partnership agreement is the source of a partnership; it also gives expression to the other ingredients defining the partnership, specifying the business agreed to be carried on, the persons who will actually carry on the business, the shares in which the profits will be divided, and the several other considerations which constitute such an organic relationship. It is permissible to say that a partnership agreement creates and defines the relation of partnership and therefore identifies the firm. If that conclusion be right, it is only a further step to hold that each partnership agreement may constitute a distinct and separate partnership and therefore distinct and separate firms. That is not to say that a firm is a corporate entity or enjoys a juristic personality in that sense. The firm name is only a collective name for the individual partners. But each partnership is a distinct relationship. The partners may be different and yet the nature of the business may be the same, the business may be different and yet the partners may be the same. An agreement between the partners to carry on a business and share its profits may be followed by a separate agreement between the same partners to carry on another business and share the profits therein. The intention may be to constitute two separate partnership and therefore two distinct firms. Or to extend merely a partnership, originally constituted to carry on one business, to the carrying on of another business. It will all depend on the intention of the partners. The intention of the partners will have to be decided with reference to the terms of the agreement and all the surrounding circumstances, including evidence as to the interlacing or interlocking of management, finance and other incidents of the respective

businesses."In McDowell & Company Ltd. v. Commercial Tax Officer (1985) 5 ECC 259 a Five Member Bench of the Hon'ble Supreme Court had the following to say - "Tax planning may be legitimate provided it is within the framework of law. ' Colourable devices cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honourable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges." 9. The facts in the present appeals may now be examined in the light of the two Supreme Court decisions referred to above and guidelines given in K. Kelukutty's case (supra). Central Excises & Salt Act, 1944 Section 2 defines "manufacture" and then goes on to say that the word manufacturer shall be construed accordingly. Rule 2 of Central Excise Rules, 1944 defines an "assessee". Rule 174 requires every manufacturer, trader or person mentioned therein to take out a licence.

In notifications issued under Rule 174A providing for general exemption from licensing control in the Schedule providing for form of application for claiming exemption reference was to proprietors/partners and directors of the company owning the factory.

There is nothing in the Central Excises & Salt Act, 1944 or Rules modifying the partnership law. Once in view of the Supreme Court decision in K. Kelukutty case it is remembered that firm name is only a collective name for the individual partners and that it is not a corporate entity or enjoys a juristic personality, partnership law in absence of any modification of the same by Central Excises & Salt Act, 1944 or Rules would have to be applied. We have already set out above that the second partnership came into existence while notifications based on value of clearances and investment on plant and machinery were operative. The first partnership dated 16.3.1977 in continuation of earlier partnership deed dated 20.5.1974 stated that the business of the firm shall be manufacturing and selling of paper packing materials and such other business as may be decided amongst the partners from time to time. Clause 3 of the partnership deed also stipulated that business of the partnership firm shall be carried at Jammu or at such place or places as may be decided from time to time by the partners. In this partnership profit and loss of the firm was to be divided amongst two partners Shri Gopal

Magotra and Shri Shrikumar Sharma in proportion of 50% each. In view of the terms and conditions of the partnership aforesaid, it is not understandable why it became necessary to constitute another firm for manufacturing and selling of paper packing materials inducting the wives of the two partners, namely, Smt. Komal Magotra and Smt. Sudesh Sharma with 25% share each. To the aspects of the wives we would come later. If terms of the partnership agreement are examined in the light of guideline set out by the Hon'ble Supreme Court i.e., surrounding circumstances, management, finance and other incidents of the respective businesses, the irresistible conclusion is that the second partnership was set up only in order to defeat the provisions of the exemption Notifications 176/77,89/79 and 105/80 set out above. While a partnership may be constituted to carry on a business, there cannot be a partnership to defeat a notification or provisions of law. Now the first partnership consisting of two husbands Shri Gopal Magotra and Shri Shrikumar Sharma i.e., M/s. Paper Packing Industries exceeded the stipulated exemption limit of rupees thirty lakhs value of clearances. These two partners have 25% share each in the profit and loss in the other partnership M/s. Packarts. The ordinary presumption would be that clearances to the extent of their share in profit and loss in this firm should be attributable to them and should be clubbed for judging their eligibility of the first firm namely Paper Packing Industries to benefit of exemption under the notification.

10. As for the two wives, namely, Smt. Komal and Smt. Sudesh there may be cases where the clearances attributable to wives based on their share in profit and loss or investment may be relatable to them and may not be clubbable with the clearances of their husbands but in order that it be so, necessary pleading and evidence should be there. From the order of the Assistant Collector of Central Excise it appears that these two wives had executed power of attorney in favour of their husbands and had no role to play in the business of the second firm. We have already set out above how the second partnership came into existence only in order to defeat the provisions of notification and how this may not be legal. It appears that the two wives with 25% share each in profit and loss were inducted into the second partnership in order to avoid the allegation that the clearances of the firm were in fact for and on behalf of the first firm constituted by the two husbands which had exceeded the clearance limit, the clearance being in the

order of rupees sixty lakhs. If such a position be accepted then law would be defeated and tax avoided by co-opting one or two partners and arguing that the two partnerships are distinct and different from one another. Such a subterfuge cannot be accepted in view of the Supreme Court decision (supra).

11. Considering all the relevant circumstances it appears that the clearances made by the second firm constituted by two husbands and their two wives were also for and on behalf of the first firm. The Assistant Collector in our view was right in clubbing them and denying them each separate exemption in the order of clearances to the extent of rupees thirty lakhs. In view of this finding the order of Collector (Appeals) must be set aside and the one passed by the Assistant Collector of Central Excise restored. We set aside the order of the Collector (Appeals) and restore that of the Assistant Collector.

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