

Court No. - 7

Case :- CENTRAL EXCISE APPEAL No. - 89 of 2019

Appellant :- Commissioner, Central Goods And Service Tax
Commissionerate

Respondent :- M/S International Tobacco Co. Ltd.

Counsel for Appellant :- Dhananjay Awasthi

Counsel for Respondent :- Shubham Agrawal

With

Case :- CENTRAL EXCISE APPEAL No. - 88 of 2019

Appellant :- Commissioner, Central Goods And Service Tax
Commissionerate

Respondent :- R.K. Gupta

Counsel for Appellant :- Dhananjay Awasthi

Counsel for Respondent :- Shubham Agrawal

Hon'ble Biswanath Somadder,J.

Hon'ble Ajay Bhanot,J.

[Per: Hon'ble Ajay Bhanot,J.]

1. Both the Central Excise Appeals instituted under section 35-G of the Central Excise Act, 1944 arise from the same judgment and order passed by the learned Customs, Excise & Service Tax Appellate Tribunal, Allahabad, dated 3rd April, 2018, which sets aside the Order-in-Original dated 21st October, 2010 passed by the Commissioner of Customs, Central Excise & Service Tax, Ghaziabad.

2. The appeals raise two separate substantial questions of law but the facts are the same. The substantial questions of law arising in both the appeals respectively can be decided conveniently by one judgment.

3. The learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT), Allahabad, in its order dated 03.04.2018 held that the assessee – respondent is entitled

to CENVAT credit and has lawfully taken and utilized CENVAT credit under Rule 16 of the Central Excise Rules, 2002. The Commissioner of Customs, Central Excise & Service Tax, Ghaziabad, had in the Order-in-Original dated 21st October, 2010, found that the assessee had wrongly availed of the CENVAT credit under Rule 16(1) of the Central Excise Rules, 2002 and accordingly ordered recovery of evaded liability and imposed penalty.

4. The connected Central Excise Appeal No.88 of 2019 (Commissioner, Central Goods and Service Tax Commissionerate, Ghaziabad Versus R.K. Gupta) has also been filed against the said judgment and order of the learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT), Allahabad, dated 3rd April, 2018, in regard to reversal of the penalty imposed upon Sri R.K.Gupta under Rule 26 of the Central Excise Rules, 2002 by the Order-in-Original dated 21.10.2010.

5. The respondent – assessee is engaged in the manufacture of various brands of cigarettes on job work basis for M/s Godfrey Philips India Limited. During the period under assessment, certain cigarettes manufactured and removed by the appellant on payment of Central Excise duty were returned by Godfrey Philips India Limited for various reasons. The respondent – assessee claimed that the goods were brought back to the factory for refining.

6. The respondent – assessee took CENVAT credit by

treating the said returned goods as inputs for the period November, 2006 to May, 2007 and for the period August, 2008 to April, 2009.

7. The respondent – assessee claimed entitlement to credit under Rule 16(1) of the Central Excise Rules, 2002 and availed of the CENVAT credit under Rule 16(2) of the Central Excise Rules, 2002, when the goods were removed from the factory after “refining”. Principally, the controversy in the instant appeal centres around Rule 16(1) of the Central Excise Rules, 2002.

8. When the offending transactions were noticed by the Revenue, show cause notices were issued to the respondent – assessee. The show cause notices recorded that “refining” of cigarettes is not covered under Rule 16 of the Central Excise Rules, 2002. The sum and substance of the case of the Revenue against the respondent – assessee was that the respondent – assessee engineered the return of the so-called non marketable/non saleable cigarettes, with the intent to unlawfully avail the benefits of CENVAT credit under Rule 16 (1) of the CENVAT Credit Rules, by misleading the Revenue.

9. The show cause notice specifically asserted that the respondent – assessee had wilfully, knowingly and with a mala fide intention, wrongly availed CENVAT credit which is recoverable from it under Rule 14 of the CENVAT Credit Rules, 2004, read with proviso to section 11A of the Central Excise Act, 1944, along with

interest under section 11AB of the said Act. The respondent – assessee was also liable for penal action under Rule 15(2) of the CENVAT Credit Rules, 2004, read with section 11AC of the Central Excise Act, 1944.

10. Sri R.K.Gupta is the appellant in the connected appeal who was “the sole In-charge and responsible person for day-to-day working in respect of all excise matters in the factory” was also noticed for having concealed facts to mislead the department and was liable to penal action under Rule 26 of the Central Excise Rules, 2002, read with section 11AC of the Central Excise Act, 1944.

11. The respondent – assessee showed cause and tendered its defence before the noticing authority and contested the proceedings.

12. The assessing officer adjudicated the controversy by order dated 21.10.2010 wherein it found in favour of the Revenue and held that the assessee had wrongly claimed CENVAT credit under Rule 16(1) of the Central Excise Rules, 2002 and Sri R.K.Gupta, Deputy General Manager (IT & Accounts) was liable to pay penalty under Rule 26 of the Central Excise Rules, 2002.

13. The assessing officer found that the assessee – respondent had wrongly availed CENVAT credit, amounting to Rs.6,83,28,039/- (Rupees six crores eighty three lakhs twenty eight thousand thirty nine only) under Rule 16 of the CENVAT Credit Rules, 2004.

14. A penalty to the tune of Rs.6,83,28,039/- (Rupees six crores eighty three lakhs twenty eight thousand thirty nine only) was also imposed upon the respondent – assessee.

15. A penalty of Rs.5,00,000/- (Rupees five lakhs only) was imposed on Sri R.K.Gupta in the connected appeal under Rule 26 of the Central Excise Rules, 2002. Sri R.K.Gupta suffered the penalty for his involvement in wrong availment of the above mentioned amount of CENVAT credit in contravention of the provisions of CENVAT Credit Rules, 2004, & Central Excise Act, 1944 and the Rules framed thereunder. This penalty is the subject matter of Central Excise Appeal No.88 of 2019 (Commissioner, Central Goods and Service Tax Commissionerate, Ghaziabad Versus R.K. Gupta).

16. The adjudicating authority in its Order-in-Original dated 21.10.2010 fixed the aforesaid liabilities under the CENVAT Credit Rules, 2004 and Central Excise Act, 1944 and Central Excise Rules, 2002 on the foot of such reasons as set forth hereinunder:

“6.4 From the contents of show cause notice I find that there are following basic issues raised-

(i) The cigarettes received back from sale offices or C & F agents are not returned by the said sale offices or C & F Agents against damage or defects but are returned as per guidance from ITC only for want of reasons not disclosed to the Department. It has been brought out in the notice that memos are issued to the sale offices for return of goods as per directions of ITC themselves against which the cigarettes are returned without any remarks as to why the same have been returned. The challans accompanying returned cigarettes contain note “please receive following brands of cigarettes against your order”. On receipt of cigarettes, ITC had informed the Department the reasons like “Brand not marketable”, cigarettes giving bad smell”. However, it was

found that the cigarettes of same brand which was claimed to be not marketable were again dispatched to the same sale office from where they received the returned cigarettes. In every case, ITC informed the Department that the cigarettes were received for refreshing. The cigarettes received back were found in original packing and even outer cartons were intact. It has been alleged in the SCN that the claim of the party that the same found defective were received back for refreshing is not true as even without removing the outer carton, how one can come to know that the cigarettes are not in a condition to be marketed.

(ii) The process of refreshing has been elaborated in the SCNs. It has been found that on receipt of returned cigarettes, the same are scrapped and the outer cartons, cigarette packets, cigarette wrapper, filter almost every cenvatable material on which Cenvat credit had been availed by ITC are thrown away without payment of duty. It is only the tobacco of the returned cigarettes which is recovered (to the extent of around 80%) and the same is reused for the manufacture of fresh cigarettes. It has thus been alleged that all the inputs except tobacco are separated first and disposed off and then only the tobacco portion is used in manufacturing of fresh cigarettes.

6.5 From the above I find that cigarettes received back for refreshing are not put to use as inputs for the manufacture of finished goods. These are actually put to the process of separation of all inputs other than tobacco by method of scrapping and to my opinion, the said process cannot be treated as a manufacturing process. The returned cigarettes as such can also not be treated as inputs as the same cannot be put to use as inputs in the manufacture of cigarettes. I also feel that the use of retrieved tobacco by mixing with fresh tobacco is done by the party with the sole aim to avail credit on returned goods as the value of such tobacco is very low as compared to the credit available to them on returned cigarettes.

6.6 As discussed above, the value of tobacco is comparatively much smaller as compared to the value of all other goods which are scrapped and thrown away without payment of duty. Going into the process of refreshing, I find that the entire material received back is put to scrapping process and two things are obtained namely, (1) scrapped cartons/packet/cigarette paper/ filter and (2) tobacco. The scrapped material is a non excisable material and is disposed off without payment of duty and the tobacco so recovered is put to use for the manufacture of cigarettes. Thus it is evident that the returned cigarettes are actually used in the manufacture of scrapped goods (non dutiable) and only tobacco can be said to be used in the manufacture of dutiable goods. Thus it is evident that the purpose of receipt of cigarettes is to remove them from the market stream and to destroy them and not to use them as inputs in the manufacture of fresh goods. As such I feel that the returned cigarettes do not come within the purview of rule 16 of CER, 2002 under the provisions of which ITC have availed credit on them.”

17. The respondent – assessee carried the Order-in-

Original passed by the adjudicating authority in appeal before the learned Customs, Excise and Service Tax Appellate Tribunal. The learned Customs, Excise and Service Tax Appellate Tribunal, by its judgment dated 15.10.2018, held in favour of the assessee and quashed the order passed by the adjudicating authority. The learned Appellate Tribunal found the assessee to be entitled for CENVAT credit under Rule 16(1) on the following understanding of the said Rule:-

“A bare perusal of Rule 16(1) supports the contention of the learned counsel for the Appellants inasmuch as it enacts a fiction of law to the effect that the goods on which duty has already been paid at the time of removal thereof are brought into any factory for various reasons mentioned in the Rule, including but not limited to any other reason, they are entitled to take CENVAT Credit of duty paid on such goods, as if such goods are received as inputs under the CENVAT Credit Rules, 2002 and is entitled to utilize this credit according to the said Rule. These returned cigarettes were brought back into the factory under conditions specified under Rule 16 of the Central Excise Rules, 2002 alongwith the Forwarding Challan-cum-Invoice counter signed by the Officer of the Department. From the record, we find that the adjudicating authority while coming to the conclusion in para 6.2 has observed that:

“6.2. The issue in the present proceedings before me is whether cigarettes received back from sale offices or from clearing and forwarding agents are eligible for credit of duty paid on them originally at the time of their clearance from the factory under the provisions of rule 16 of CER, 2002. I would like to analyze the provisions of this rule under which the impugned credit has been availed by the party. In terms of this rule, goods should be brought back for being re-made, refined re-conditioned or for any other reason and the assessee is entitled to take credit of duty paid if such goods are received as inputs under the Cenvat credit rules, 2002. I find that ITC, in their reply have given force on the words “for any other reason”. I find that the availment of Cenvat credit is primarily governed by CCR, 2002/2004 and thus the availment of Cenvat credit provided by any other rule like CER, 2002 cannot be beyond the provisions of Central Credit Rules. Here I also find that in the said rule 16 of CER, 2002, there is clear mention that goods must be received to be used as inputs in term of CCR, 2002. Thus the very first condition for eligibility of credit on returned goods is that the goods

must be usable and used as inputs in the manufacture of finished goods. I find that the very basis of the present dispute is that Department has alleged that the goods have not been brought back for being used as inputs but only to take credit in the guise of rule 16 of CER, 2002. On the other hand, ITC have stressed that conditions of Rule 16 of CER, 2002 have been satisfied by them for availment of credit on returned cigarettes.”

From the above, we find that the reasoning given by the adjudicating authority with respect to Rule 16 is by assuming that it deals with inputs “as such” and not inputs “as if”.

6. We further find that Rule 16 is wide enough to cover the case of the Appellants in view of the wordings used in it which inter alia includes “any other reason” for receiving the duty paid goods. The duty paid character of the goods, being not disputed in the present case, Rule 16 is squarely applicable and accordingly the Appellants have rightly taken the CENVAT Credit and utilized the same.”

18. The following are the substantial questions of law which fall for determination in these appeals:

1. “Whether the learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT) was misdirected in law in its interpretation of Rule 16 (1) of the Central Excise Rules, 2002, by unlawfully including scrapping within the scope of Rule 16(1) of the Central Excise Rules, 2002 ? Further, whether the learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT) erred in law by finding that the respondent – assessee had lawfully availed CENVAT credit in the offending transactions ?”

2. “Whether the learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT) was justified in law to revoke the penalty imposed upon the appellant under Rule 26 of the Rules by the Order-in-Original dated 21st October, 2010 ?”

19. Rule 16(1) is germane to the controversy and thus needs careful consideration. For ease of reference, Rule

16 (1) of the Central Excise Rules, 2002, is being extracted in its entirety:

“Rule 16. Credit of duty on goods brought to the factory. – (1) Where any goods on which duty had been paid at the time of removal thereof are brought to any factory for being re-made, refined, re-conditioned or for any other reason, the assessee shall state the particulars of such receipt in his records and shall be entitled to take CENVAT credit of the duty paid as if such goods are received as inputs under the CENVAT Credit Rules, 2002 and utilise this credit according to the said rules.”

20. Rule 16 states the procedure and eligibility to avail credit of duty on goods brought to the factory. Various ingredients of Rule 16(1) will now be discussed.

21. Rule 16(1) is applicable to goods on which duty had been paid at the time of removal of such goods and the same are brought back to the factory. The goods are brought back to the factory for being “re-made, refined, re-conditioned or for any other reason”. The assessee is also required to state the particulars of such receipt of goods in his records.

22. Once the above conditions are fulfilled, the assessee becomes entitled under Rule 16(1) to take CENVAT credit of the duty paid on the returned goods as if such goods are received as inputs under the CENVAT Credit Rules, 2002. The credit shall be utilised by the assessee according to the latter Rules.

23. The purpose of manufacture of goods in this case is sale. Bringing the goods back to the factory after they have been removed for sale does not ordinarily make good business sense. However, at times for some valid reasons, the goods cannot be sold or they are not fit for retention in the market. In such circumstances, the goods

may be recalled and brought to the factory. In terms of Rule 16(1), these goods are brought to the factory for being “re-made, refined, re-conditioned or for any other reason”. After being subjected to said processes, the goods are again removed having become saleable commodities and worthy of acceptance in the market.

24. The phrase “or for any other reason”, in Rule 16(1) of the Central Excise Rules, 2002, has to be necessarily read on the construction canon of *ejusdem generis*. Any other rule of interpretation would make the Rule unworkable and defeat the clear intention of the legislature.

25. The learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT), proceeded to give a wide interpretation to the phrase “or for any other reason” and thus included the offending transaction within its scope. The legislative intent was not to read the phrase in isolation and give it such a wide berth. Otherwise, there would be no necessity to precede the phrase “or for any other reason” by the three processes of “re-made”, “refined” and “re-conditioned”. The three preceding phrases depicting three similar processes qualify and restrict the scope of the phrase “or for any other reason”.

26. While explaining the concept of *ejusdem generis* this Court in ***Special Appeal No.33 of 2019 in Gyanwati Devi v State of U.P. and 5 others*** held:

“The reason is, when a general word or phrase follows a list of specifics, the general word or phrase will be interpreted to include only items of the same class as those already listed.”

27. The phrase “for any other reason” has to be interpreted in light of the preceding expressions of “re-made, refined, re-conditioned”. The processes coming under the category of “for any other reason”, have to be in the likeness of the processes which immediately precede the aforesaid phrase. All the processes should have such similarities so as to be constituted into the same class.

28. The legislature has employed the words “re-made”, “refined”, “re-conditioned” and the phrase, “or for any other reason” and eschewed the phrase “for being scrapped”. Understanding this distinction is the key to interpreting the scope of “re-made”, “refined”, “re-conditioned” and the phrase, “or for any other reason”.

29. The essential characteristics of the brought back goods survive even after they are “re-made”, “refined” or “re-conditioned”. The original identity of the goods is retained even after the goods undergo the said processes.

30. When goods are scrapped, all the constituent components of the goods may be reclaimed. After scrapping, the original identity of the manufactured goods completely perishes. Scrapping of goods is done for various purposes, including cannibalisation and extraction of vital or valuable parts of the original goods.

31. “Re-made”, “refined” and “re-conditioned” are processes akin to manufacture; while scrapping involves destruction of the original identity of the goods. Scrapping is neither a species nor in the likeness of “re-

made”, “refined” or “re-conditioned”. Consequently, when goods are scrapped, it cannot be stated that the said goods were brought to the factory for being “re-made”, “refined”, “re-conditioned”, “or for any other reason” provided in Rule 16(1). Scrapping of goods does not fall within the ambit and scope of Rule 16(1).

32. Ordinary business prudence requires that valid commercial reasons must exist for bringing the goods back to the factory. The validity of these reasons is the test of the bona fides of the assessee. These can be ascertained from authentic records, relating to receipts of goods and particulars contained therein. Scrutiny of such records and the contents of the receipts will help determine the bona fides of the assessee to bring back the goods.

33. Offending transactions and the findings of the Assessing Officer as well as learned Appellate Tribunal have to be examined in the light of the true scope and correct interpretation of Rule 16(1), as stated in the preceding paragraphs of this judgment.

34. We find that the learned Appellate Tribunal, while interpreting the phrase, “any other reason”, in Rule 16(1) and held that the same was “wide enough to cover the case of the appellants”. Consequentially, the learned appellate Tribunal included scrapping within the fold of Rule 16(1).

35. It is evident that the learned Appellate Tribunal has incorrectly interpreted the scope of Rule 16(1) by

bringing scrapping within the embrace of Rule 16(1) and has proceeded to legitimise the benefit of CENVAT availed by the respondent – assessee. These fault-lines vitiate the judgment of the learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT), Allahabad. The judgment of the learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT), Allahabad, is therefore unsustainable in law.

36. The findings of facts returned by the Assessing Officer thus attain finality since they were not successfully impeached by the learned Appellate Tribunal. These findings extracted in extenso in the earlier part of the judgment are set forth, in brief, hereinafter to take the discussion forward and to its logical conclusion.

37. The cartons containing cigarettes were not even opened and found in packed condition. The alleged defects in goods, as claimed by the assessee, thus could not be ascertained without opening the cartons. The goods were actually sent back to the same purchasers in the self-same condition in which they were received.

38. The receipts were not found to be reliable. There are no records of the reasons given by the purchasers for rejecting the consignments of goods. On this foot, the reasons for bringing back the goods to the factory, as adduced by the assessee, were disbelieved.

39. The scrapping of the goods stood established by reliable evidence and cogent findings in the record. The

assessee, in fact, scrapped the goods and tried to pass it as “refining” the goods.

40. Clearly, the goods were not brought back to the factory by the assessee to be “re-made”, “refined”, “re-conditioned”, “or for any other reason” as contemplated in Rule 16(1) of the Central Excise Rules, 2002. The transactions were devices to illegally avail CENVAT credit. The intent to illegal avail CENVAT credit and escape duty was fully established.

41. In wake of the preceding narrative, we find that the ingredients to avail credit of duty of goods brought back to the factory, as contemplated under Rule 16(1) of the Central Excise Rules, 2002, were not satisfied. The assessee was not entitled to avail the benefit of CENVAT credit of the duty paid on the aforesaid goods and illegally availed such credit. The intent of the assessee to defraud the revenue and escape tax is thus proved.

42. The controversy in the connected Central Excise Appeal No.88 of 2019 (Commissioner, Central Goods and Service Tax Commissionerate, Ghaziabad Versus R.K. Gupta) in respect of imposition of penalty upon Sri R.K.Gupta turns on the construction of and observance of the ingredients of Rule 26 of the Central Excise Rules, 2002. For facility of reference, Rule 26 is extracted hereunder:-

“RULE 26. Penalty for certain offences. — (1) Any person who acquires possession of, or is in any way concerned in transporting, removing, depositing, keeping, concealing, selling or purchasing, or in any other manner deals with, any excisable goods which he knows or has reason to believe are liable to confiscation under the Act or these rules, shall be liable to a penalty not exceeding the duty on such goods or [two thousand rupees],

whichever is greater:

(2) Any person, who issues-

(i) an excise duty invoice without delivery of the goods specified therein or abets in making such invoice; or

(ii) any other document or abets in making such document, on the basis of which the user of said invoice or document is likely to take or has taken any ineligible benefit under the Act or the rules made thereunder like claiming of CENVAT credit under the CENVAT Credit Rules, 2004 or refund, shall be liable to a penalty not exceeding the amount of such benefit or five thousand rupees, whichever is greater.”

43. Rule 26 of the Central Excise Rules, 2002, has to be read in conjunction with the findings of facts narrated in the preceding part of the judgment. The ingredients of Rule 26 for imposing the penalty upon Sri R.K.Gupta, Deputy General Manager (IT & Accounts), are fully satisfied. The provisions of the Rule 26 have been duly adhered to. The order imposing penalty against Sri R.K.Gupta under Rule 26, is a lawful and just order, in the facts and circumstances of this case.

44. Accordingly, the substantial questions of law are answered against the assessee and in favour of the Revenue in the following terms:-

I. The learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT) was clearly misdirected in law in its interpretation of Rule 16(1) of the Central Excise Rules, 2002 by unlawfully including “scrapping” within the scope of Rule 16(1) of the Central Excise Rules, 2002. The learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT) also erred in law by finding that the respondent – assessee had lawfully availed CENVAT credit in the offending transaction.

II. The learned Customs, Excise & Service Tax Appellate

Tribunal (CESTAT) was completely unjustified in law by setting aside the penalty imposed upon R.K. Gupta, in connected Central Excise Appeal No.88 of 2019 (Commissioner, Central Goods and Service Tax Commissionerate, Ghaziabad Versus R.K. Gupta), even in the face of the fact that the ingredients of Rule 26 of the Central Excise Rules, 2002, were fully satisfied. R.K.Gupta, in law, was liable to pay the penalty imposed in the Order-in-Original passed by the Commissioner of Customs, Central Excise & Service Tax, Ghaziabad.

46. As a consequence, the judgment of the learned Customs, Excise & Service Tax Appellate Tribunal (CESTAT), Allahabad, dated 3rd April, 2018, is liable to be set aside and is set aside. The judgment of the Commissioner of Customs, Central Excise & Service Tax, Ghaziabad, dated 21st October, 2010, is upheld to the extent and manner indicated in the body of this judgment.

47. Both the appeals are accordingly allowed.

Order Date :- 6.12.019
Ashish Tripathi

(Biswanath Somadder,J.)

(Ajay Bhanot,J.)