(1980) 08 BOM CK 0003

In the Bombay High Court

Case No : Special Civil Application No. 2673 of 1976

Amar Dye-chem. Ltd. and another APPELLANT

Vs

Union of India and another RESPONDENT

Date of Decision : 05-08-1980

Acts Referred:

Central Excises and Salt Act, 1944 — Section 2, 4, 4(1), 4(4)

Citation : (1981) 8 ELT 348

Hon'ble Judges : R.S. Bhonsale, J;M.N. Chandurkar, J

Bench : Division Bench

Judgement

Chandurkar, J.—Petitioner No. 1 is a company which inter alia carries on business of manufacture of various chemicals and dyes and the chemicals with which we are concerned in this petition fall under Tariff Items Nos. 14D, 14DD and 15A under the Central Excises and Salt Act, 1944 (hereinafter referred to as "the Act"). Petitioner No. 2 is one of the Directors of petitioner No. 1 (hereinafter referred to as "the manufacturer").

2. The manufacturer filed from time to time price lists in the prescribed forms for the goods sold by it. The manufacturer has been entering into agreements with what are described as distributing agents for the purpose of sale and of distribution of the goods manufactured by it and specimen copy of the agreement has been filed along with the petition. Upto 1st October, 1975 the price lists which were filed by the manufacturer with the Central Excise Authorities and which were duly approved by them did not include the trade discount allowed to the distributing agents under the terms and conditions of the agreement with the distributing agents.

3. By the Central Excises and Salt Amendment Act, 1973, old section 4 was substituted by new section 4 in the Act. The Amending Act came into force from 1st October, 1975. The manufacturer filed fresh price lists in Part I in the new form which was prescribed after the amendment of the Act. The petitioners submitted complete price lists effective from 1st October, 1975 in the new

proforma I, and informed the authorities that they were operating uniform price and discount for all their distributors, subsidiary companies and associate companies and that, therefore, the price lists were being submitted only in form 1. The petitioners requested that the said price lists should be approved.

4. It has now been stated before us that though these forwarding letters refers to distributors, subsidiary companies and associate companies, there are no sales or transactions in respect of the Tariff item in question to or with any subsidiary or associate companies. The price list is approved by the Central Excise Authorities on 30th September, 1975. It, however, appears that the Excise Department changed its mind and by letter dated 8th October, 1975 the Assistant Collector, Central Excise, Kalyan, intimated to the manufacturer :

"The approval accorded to the price list should be treated as withdrawn since the goods are generally not sold by you in the course of wholesale trade except to or through related person viz. distributors, subsidiary companies and associated companies as indicated in your letter referred to above and hence the proper proforma for you to declare your price is Part IV and not Part I."

The letter seems to be restricted to the price list of synthetic resins, which is Tariff Item 15A. The Assistant Collector drew the attention of the manufacturer to the definition of the term "related person" in section 4(4) of the Act. The letter, however, made it further clear that the same order would apply to the price list in respect of the other goods manufactured and cleared by the assessee for which he had filed a price list in Part I of the proforma.

5. The manufacturer in compliance with the directions of the Assistant Collector submitted a revised price list in Part IV under protest and without prejudice to its rights to seek recourse, "to legal channel".

6. The Assistant Collector further informed the manufacturer by his letter dated 20th December, 1975 that the manufacturer should file as many copies of the printed list of distributors as the number of excisable commodities sold to the sub-agents.

7. The manufacturer addressed a further communication to the Assistant Collector on 24th January, 1976 informing the Assistant Collector that the distributors were in fact purchasers of the goods and the transactions with the distributors were transactions of sale and purchase and satisfied the definition of ''sale'' and ''purchase'' in section 2(h) of the Act. It was also pointed out to the Assistant Collector that the distributors who buy goods were not relatives and the price was the sole consideration for the sale and the transactions being at arm''s length, the distributors cannot be categorised as a related person as envisaged u/s 4(4)(c) of the Act. The Assistant Collector was informed by the manufacturer that they were approaching the High Court in the matter. That is how this petition has now come to be filed, in which the manufacturer has challenged the action of the Assistant Collector of withdrawing the approval given to the price lists originally filed on 12th September, 1975 and by which also a

further direction was given to the manufacturer that the new price list in Part IV should be filed.

8. Before we go to the contentions advanced before us on behalf of the manufacturer by Mr. Cooper, it is necessary to refer to certain provisions made in section 4 which became effective from 1st October, 1975. The Relevant parts of section 4 with which we are concerned in this petition read as follows :

Section 4 "Valuation of excisable goods for purposes of charging of duty of excise.

(1) Where under this Act, the duty of excise is chargeable on any excisable goods with reference to value, such value shall subject to the other provisions of this section, be deemed to be -

(a) the normal price thereof, that is to say, the price at which such goods are ordinarily sold by the assessee to a buyer in the course of wholesale trade for delivery at the time and place of removal, where the buyer is not a related person and the price is the sole consideration for the sale :

Provided that -

(i) ....

(ii) ....

(iii) .... Where the assessee so arranges that the goods are generally not sold by him in the course of wholesale trade except to or through a related person, the normal price of the goods sold by the assessee to or through such related person shall be deemed to the the price at which they are ordinarily sold by the related person in the course of wholesale trade at the time of removal, to dealers (not being related persons) or where such goods are not sold to such dealers, to dealers (being related persons) who sell such goods in retail.

(2) ....

(3) ....

(4) For the purposes of this section,

(a) ....

(b) ....

(c) ...... ''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".

Under the amended provision in section 4 of the Act, the value of the excisable goods for the purpose of chargeability to duty of excise is under clause (a) of section 4(1) deemed to be the normal price of the excisable goods. Under clause (a) this normal price is stated to be the price at which such goods are ordinarily sold by the assessee to a buyer in the course of a wholesale trade for delivery at the time and place of removal where the buyer is not a related person and the price is the sole consideration for the same. In other words, the concept of normal price which is now introduced by section 4(1) requires the determination of the price at which goods are ordinarily sold by the assessee to a buyer who is not a related person and the sale must be in the course of wholesale trade and price must be the sole consideration for the sale. The point of time with reference to which the price has to be determined is the time of delivery of the excisable goods in the course of wholesale trade and such price has to be determined with reference to the place of removal of the goods. The related person referred to in clause (a) is defined in section 4(4)(c) of the Act as reproduced above. The definition appears to be in two parts, the letter being an inclusive part. Under the first part of the definition, a person who is so associated with the assessee that they have interest, directly or indirectly, in the business of each other is defined as a related person. In the latter inclusive part of the definition, a holding company, a subsidiary, a relative and a distributor of the assessee and any sub-distributor of such distributor is included in the definition of a related person. Under the Explanation to clause (c), the terms ''holding company'', ''subsidiary company'' and ''relative'' are given the same meanings as in the Companies Act, 1956. As already pointed out, we are not in this case concerned with either a holding company or a subsidiary company, nor are we concerned with a relative. We are also not concerned with the first part of the definition of related person. We are concerned with the meaning of a distributor who is included in the definition of a related person. Now, the scheme of section 4 appears to be that where the buyer is a related person, then the normal price has to be determined in the manner provided in the third proviso to section 4(1)(a) of the Act. Under the third proviso, it is provided that where the assessee so arrange that the goods are generally sold by him in the course of wholesale trade except to or through a related person, the normal price of the goods sold by the assessee to or through such related person shall be deemed to be the price at which they are ordinarily sold by the related person in the course of wholesale trade at the time of removal, to dealers (not being related persons) or where such goods are not sold to such dealers, to dealers (being related persons) who sell such goods in retail". The effect of this proviso is that for the purposes of chargeability to excise duty the normal price is not the price at which the manufacturer sells to any of the persons who fall within the definition of a related person but that excise duty is required to be charged with reference to the price at which the related person sells to dealers who are not related persons in the course of wholesale trade at the time of removal. The latter of the provisions refers to a case where the goods are not sold to dealer who is also a related person and in such a case, the normal price is the price at which such a dealer who is a related person sells such goods in retail.

9. Now, with this scheme of the material provisions, so far as the present case is concerned, we will notice the contentions which have been raised on behalf of

the petitioners in this case. The first contention is that section 4(1)(a) read with the third proviso, in the case of a person who falls within the definition of a related person, seeks to levy a charge of excise duty on a price which is bound to be in excess of the manufacturing cost and the manufacturing profit because, according to the learned Counsel, where the third provision is sought to be invoked by the Excise Department, the value of the excisable article is determined not with reference to the wholesale price charged by the manufacturer to a related person but with reference to the price which a related person charges to the wholesale buyer. This, according to the learned Counsel, turns counter to the basic concept of excise duty propounded from time to time by the Supreme Court and by several other Courts and the duty ceases under the third proviso to be a duty on the manufacturer of an article. The learned Counsel, therefore, contends that the third proviso should be declared to be ultra vires the powers of the Parliament, as has been done by the Gujarat High Court in Cibatul Limited v. Union of India and others - 1979 E.L.T. (J 407). It may be pointed out that the Division Bench of the Gujarat High Court has in Cibatul Limited case struck down proviso (iii) to clause (a) of sub-section (1) of section 4 as ultra vires the Parliament''s legislative competence under Article 246 read with Entry 84 in the Union List and Entry 54 in the State List. Referring to the provisions of section 4(1)(a) of the Act, the Gujarat High Court has pointed out that in the case of a sale to a related person, the Parliament by amending section 4 directs the authorities to ignore the fully commercial first price consisting of manufacturing costs and manufacturing profits and to take into account the second or subsequent price and it encroached upon Entry 54 in the State List, upon which it cannot legislate by virtue of the provisions of Article 246(3) of the Constitution. In paragraph 33 of the Judgment, the Gujarat High Court has observed as follows :-

"It is, therefore, clear that the concept of ''related person'' brings by itself something in respect of which Parliament lacks power to legislate. ''Related Person'' or ''no related person'' Parliament can levy excise duty only on assessable value of ''excisable goods'' made up of manufacturing costs and manufacturing profits. It cannot levy excise duty upon anything else. Therefore merely because the manufacturer''s sale of his excisable goods is to a ''related person'', it cannot be assumed that what the ''related person'' has paid to the manufacturer is not a fully commercial price. In our opinion, therefore, the expression ''the buyer is not a related person'' appearing in clause (a) of sub-section (1) of section 4 of the Excise Act, is ultra vires the legislative competence of Parliament under Art. 246 read with entry 84 in the Union List and in light of entry 54 in the State List".

Thus after declaring a part of section 4(1)(a), which introduced the concept of a sale not being to a related person, as ultra vires, the Gujarat High Court went on to consider the validity of the third proviso which was also struck down as invalid. Dealing with the third proviso to section 4(1)(a) after declaring a part of section 4(1)(a) as invalid, the Gujarat High Court in paragraph 34 has observed as follows :-

"Proviso (iii) to clause (a) of sub-section (1) of Section 4 also suffers from the same vice. It does not matter whether the assessee arranges to sell his excisable goods in the course of wholesale trade at the time of their removal to or through a ''related person'' if such ''related person'' pays the price which wholly reflects manufacturing costs and manufacturing profits. Merely because a manufacturer has sold the goods to a ''related person'', it does not mean that the price which he paid even though it is a fully commercial price should be ignored and that the second price should be taken into account. Therefore, ''related person'' or no ''related person'' as long as the manufacturer charges his buyer a fully commercial price, reflecting manufacturing costs and manufacturing profits, it ought to be taken into account for the purpose of determining the assessable value for excise duty".

Having made these observations, the Division Bench observed further in paragraph 36 as follows :-

"Proviso (iii) to clause (a) of sub-section (1) of section 4 is ultra vires the Parliament''s legislative competence under Art 246 read with entry 84 in the Union List and entry 54 in the State List, because, even though the manufacturer has charged his buyer - a ''related person'' - a fully commercial price consisting of manufacturing costs and manufacturing profits, he is liable to pay excise duty on the second price which his buyer ''related person'' - charges his buyer - an unrelated person. The second price as observed above, is loaded with the selling costs and selling profits of the manufacturer''s buyer - a ''related person''. Assessment of excise duty on selling costs and selling profits with which the assessable value is loaded partakes of Sales-tax which falls under entry 54 in the State List".

10. Mr. Cooper has thus contended both on the manner in which proviso (iii) is worked and the effect thereof that the Excise Authorities by directing the manufacturer to furnish a price list in Part IV are in effect wanting to charge excise duty not on the manufacturing costs and the manufacturing profits when the manufactured goods are sold at a commercial price to the distributors by the manufacturer but that the Excise Authorities want to charge excise duty on the price which the distributor charges to his buyer, which is bound to be loaded with post-manufacturing expenses which may have to be incurred by the distributor and which the distributor will include in the wholesale price which he will charge to his buyer. The learned Counsel, therefore, contended that the provisions in proviso (iii) should be struck down as also the clause "where the buyer is not a related person" in section 4(1)(a) should be struck down.

11. The Second contention raised before us, and the decision on which, in our view, is sufficient for the disposal of this petition, is that the word ''distributor used in the definition of "related person" is section 4(4)(c) of the Act does not include a buyer from the manufacturer who purchases manufactured goods in

wholesale in a transaction which is a transaction as between principal and principal. The learned Counsel has contended that the distributors to whom the manufacturer sells goods are not agents of the manufacturers and when they further sell goods to their buyers the sale is not on account of the manufacturer but that the sale is on account of the distributor himself. In other words, the contention is that the distributor included in the definition of a related person contemplates an agent who distributes goods to the consumers on behalf of the manufacturer and that the distributor does not include a buyer of goods from the manufacturer. In support of this argument, the learned Counsel has relied on a decision of the Allahabad High Court in Messrs. Hind Lamps Ltd. v. Union of India - 1977 Excise Law Times (J 1), and a decision of a learned singly Judge of this Court in S.M. Chemicals and Electronics and another v. R. Parthasarathy and others - 1980 Excise Law times 197.

12. Mr. Govilkar who appears on behalf of the Union of India initially objected to the specimen agreement being produced in this petition and, according to the learned Counsel, the question as to whether a particular buyer is a distributor or not is a question of fact and since the authorities were not called upon at any stage to decide whether a particular buyer fell within the definition of related person, the matter should not be gone into for the first time in this petition.

13. We have repeatedly tried to enquire from Mr. Govilkar as to what was a material on the basis of which the Assistant Collector was persuaded to withdraw the approval which was originally granted to the price list and Mr. Govilkar has fairly told us that the letter dated 8th October, 1975 was issued on the basis of the forwarding letter by the manufacturer was operating uniform price and discount "for all our distributors, subsidiary companies and associate companies". The learned Counsel had to admit that beyond looking at this letter, no further enquiry was made by the Assistant Collector and the sole foundation of the letter dated 8th October, 1975 was the fact that the distributors, subsidiary companies and associate companies fell within the definition of related person and that was why the manufacturer was directed to file a fresh price list in accordance with the third proviso in Part IV. It is obvious, therefore, that when the letter dated 8th October, 1975 was issued, it was issued by the Assistant Collector merely by looking at the definition of a related person in section 4(4)(c) of the Act. As a matter of fact at one stage the learned Counsel for the Union of India expressed his inability to put any other matter on record in support of the view taken in the letter of 8the October, 1975 except the manufacturer''s letter dated 12th September, 1975 and the definition in section 4(4)(c) of the Act. If this be the situation in which the letter dated 8th October, 1975 has been issued, it is difficult for us to entertain any objection on behalf of the Union of India that the petitioners must not be allowed to agitate in this petition a case that the distributors to whom the goods are sold by the manufacturer were not related person as contemplated by the definition in section 4(4)(c).

14. The crucial question which we must decide - at the outset before we go to

the challenge to a part of the provision in section 4(1)(a) and in the third proviso to that section is what to the scope of the concept of the distributor who is included in the definition of a related person in section 4(4)(c). It is necessary at this stage to point out that a distributor in the commercial world is understood to be a person who distributes goods of the manufacturer to the consumers and in so doing, he acts for and on behalf of the manufacturer. A distributor normally is, therefore, an agent of the manufacturer for the purpose of reaching out the goods to the consumers. The transaction between the distributor and the manufacturer in such a case is not a transaction of sale as a principal to a principal, but the distributor is in effect an agent who acts for and on behalf of the manufacturer. Such a distributor who acts for and on behalf of the manufacturer and probably earns something which is generally recognised in the commercial world as commission is not a buyer of goods from the manufacturer on his own account. Such a distributor does not himself pay price for the goods purchased before the goods are passed on to the consumers. However, in the case of a buyer who purchases goods on payment of a commercial price to the manufacturer and the transaction is in effect a sale, such a buyer is different from the kind of distributor earlier noticed though even such a buyer is sometimes described as a distributor. The distributor in such a case is in fact a wholesale buyer and the property in the goods passes to such a buyer. It is wholly immaterial whether the price is paid in cash or the goods are supplied on credit. We must not, therefore, go merely by the use of the word ''distributor'' used by the petitioner-manufacturer in the price list or in the forwarding letter. What will have to be ascertained in order to find out whether a distributor falls within the definition of related person is the real substance of the transaction between the manufacturer and the so-called distributor. We may point out that the sense in which the word ''distributor'' has been used in the definition of related person has been considered by a Division Bench of the Allahabad High Court in the Hind Lamps case cited supra. In paragraph 24 of the judgment, the Division Bench has observed as follows :-

"The word ''distributor'' is understood in commerce as an agent or one who distributes goods to consumers."

In Hind Lamps case, the Hind Lamps Company was a company registered in India, and the five shareholders of that company were :

(1) Bajaj Electricals Ltd., Bombay,

(2) Crompton Parkinson Ltd., London,

(3) N.V. Philips, Eindhovan (Holland),

(4) General Electric Co. Ltd., London, and

(5) Mazda Lamp Co. Ltd., Licester, England.

The last four of the companies were foreign companies. The Hind Lamps Company was engaged in the manufacture of electric lamps, fluorescent lamps and miniature lamps and the entire output was sold exclusively to five companies, namely, Bajaj Electricals Ltd., Philips India Ltd., Crompton Greaves Ltd., General Electric Co. of India Ltd., Mazda Lamps Co. Ltd. The manufacturer, Hind Lamps Co., put the brand names or trade marks like Philips, Osram, Mazda, Crompton and Bajaj of the respective customer companies, according to their directions and these customer companies in their turn sold these lamps under their names at prices higher than the prices charged by the petitioner company. After the coming into force of new section 4 of the Act, the Excise Department sought to levy excise duty not on the price charged by the manufacturer to the customer companies but on the prices charged by the customer companies when they sold the goods to wholesale dealers. The contention on behalf of the Excise Department was that the five customer companies came within the ambit of the term "related person" as defined in section 4(4)(c) and that the sales by the petitioner company of its products to the five customer companies also came within the scope of clause (iii) of the proviso to section 4(1)(a) of the Act and hence the value of the product for the purpose of levy of excise duty would be the price at which the customer companies sold those products in the course of wholesale trade and not the price at which the petitioner company sold those products to the five customer companies. Thus while dealing with the contention as to whether the customer companies fell within the definition of related person, the Division Bench observed as follows :-

"The word ''distributor'' is understood in commerce as an agent or one who distributes goods to consumers. It is not the case of the Central Excise Authorities that the five Customer Companies are the agents of the petitioner company. The Customer Companies are not distributing the product of the petitioner company to consumers, but generally sell to wholesale dealers. It is also not the case of the Central Excise authorities that the Customer Companies are the distributors of the petitioner company".

Having so held, the Division Bench further observed that the Central Excise Authorities could not treat the price at which the five customer companies sell the product to wholesale dealers or to the public as the value thereof for the purpose as levy of excise duty on the petitioner company.

15. Referring to the decision of the Allahabad High Court, a learned singly Judge of this Court in S.M. Chemicals & Electronics case cited supra found on facts of the case before him that the five buyers in that case did not have relationship of agent and principal for the manufacturers.

16. Though it is no doubt true that the specimen agreement filed in the present case referred to the buyer as a distributing agent, yet, as pointed out earlier, the nomenclature is not conclusive of the relationship between the manufacturer and the distributor. We have been informed that copies of such agreements are already with the Department and indeed it does appear that even the names of the distributors of the sold selling agents for which space is provided in column 8 of the price list are already with the Department. In clause 10 of this agreement,

parties have made it expressly clear that "this contract is a contract between the company and the distributing agent as principal to principal", though it is contended on behalf of the Union of India by Mr. Govilkar that the agreement is in substance an agreement of agency because the manufacturer exercises a certain amount of control over the distributor who is made responsible for the collection of prices of goods sold to nominees of the distributor. Now, we may at once point out that so far as the present case is concerned, we are concerned with transactions between the manufacturers and the distributors themselves and not between the manufacturer and a person or a dealer to whom goods have been supplied at the request of the distributor. The second clause of the agreement provides that the goods on leaving the godown at Bombay will be at the risk of the distributing agents and that it is the duty of the distributing agents to insure the goods against all risks. The distributing agent is liable to pay interest at the rate of 12% p.a. on the amount of the price remaining unpaid after 60 days. There are no doubt certain clauses in the agreement which enable the manufacturer to deal directly with the dealers in respect of transactions from which the distributing agent may be able to earn some commission. For example, in clause 11 it is provided that if the distributing agent is unable to book business for any reason whatsoever, the company reserves the right to issue direct invoices, to the party and in that case, the distributing agent''s commission will be reduced to half. However, attention may be drawn to clause 10 of the agreement also which provides as follows :-

"The Distributing Agents shall be responsible for realisation of the sale proceeds for invoices made by the Company to their clients and the Distributing Agents agree to indemnify the company for default in payment of sale proceeds to the Company by their clients or on their failure to return the documents within a week from the due date and shall also indemnify the Company for any damages sustained for such default. This Contract is a Contract between the Company and the Distributing Agent as Principal to Principal".

As already pointed out, we are concerned only with the transactions between the manufacturer and the distributing agent who in the present case is really a wholesale buyer. The price lists which were originally submitted were in respect of only such transactions of sale between the manufacturer and the distributing agents who have to obtain supplies of goods against payment in cash or against Demand Drafts and documents through recognised bankers. (See clause 2 of Ex. A). The present dispute is only in respect of such transactions between the manufacturers and the distributing agents. It is, therefore, difficult to read this agreement as constituting the distributing agent as an agent in the sense in which it is normally used in a commercial transaction. The price is paid by the distributor in his capacity as a buyer. Sales to such a buyer will fall within the main part of Sec. 4(1)(a) and such a buyer cannot fall within the category of a "related person". If such a distributor does not fall within the definition of related person, it is difficult for us to uphold the action of the Department in revoking the approval of the price list.

17. In the view which we have taken of the nature of the transactions between the petitioner company and the wholesale buyers who are described as "distributing agents" under the agreement, it is not necessary for us in this case to go into the further question as to whether any part of section 4(1)(a) of the Act can be challenged as invalid. That question would have arisen only if the distributors of the manufacturer would have fallen within the definition of a related person and then the question as to whether the manufacturer could be required to submit a price list in respect of the price at which the distributor sold wholesale to his buyer was relevant for the purposes of section 4(1)(a) read with the third clause of the proviso to that section. We are, therefore, leaving open the question about the validity of the provisions in the third clause of the proviso to section 4(1)(a) as also the question as to the validity of the part of section 4(1)(a) which has been declared invalid by the Gujarat High Court. The decision on the question as to whether the distributor falls within the definition of a related person is sufficient for the disposal of this petition.

18. In the view which we have taken, we must quash the direction dated 8th October, 1975 issued by the Assistant Collector of Central Excise, Kalyan Division, withdrawing the approval to the price list submitted by the manufacturer as being effective from 1st October, 1975. Consequently, the manufacturer will be entitled to refund of such amount as may now be found to have been paid in excess as a result of their being required to furnish fresh price list. The petitioners will be entitled to interest at 6% p.a. on the amount to the refund of which the petitioners will be found entitled from 2nd April, 1976, on which date the petition has been filed. The petitioners will be entitled to the costs of this petition. We hope that the claim for refund will be finalised within a period of three months from today.

19. Counsel for Union of India applies for leave to appeal to the Supreme Court. Leave refused.

